

An aerial photograph of a city street intersection. The street has multiple lanes, including a green-painted bike lane and a red-painted bus lane. There are several cars, a red bus, and a white truck on the road. A crosswalk with white stripes is visible. To the left, there is a parking lot with several cars and palm trees. The text "California Policy Options 2017" is overlaid in large black font on the left side of the image.

# California Policy Options 2017

**UCLA** Luskin School *of* Public Affairs  
Lewis Center



**2017**

**California**

**Policy**

**Options**

**Edited by Daniel J.B. Mitchell**

**UCLA** Luskin School *of* Public Affairs

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Lewis Center

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# Preface

For two decades, *California Policy Options* has informed researchers and journalists, as well as leaders and lawmakers, with a timely collection of research and policy recommendations on issues and opportunities in the state. The annual publication advances research solutions and policy recommendations for many of California's urban and regional challenges. These challenges include the state's economy and its governance as well as a range of issues important to the millions who call California home: business and employment, health and safety, education, transportation, housing and the environment to name a few.

Professor Daniel J.B. Mitchell, longtime editor of the series, has assembled a new collection of California-focused articles which also provides an important source of readings for Luskin students enrolled in the School's California Policy Issues course. The course, integral to the Luskin School's undergraduate Public Affairs program, is co-taught each year by Prof. Mitchell and Visiting Professor Michael Dukakis, who also has taught at the school for more than 20 years.

Heading into its third decade, *California Policy Options* will continue to providing analysis of the state's public policy problems from a variety of viewpoints as well as their political, economic and historic contexts.

**Gary Segura**

Dean, UCLA Luskin School of Public Affairs

# Introduction

Weighing in on state policy issues and the outlook for 2017 was complicated by the 2016 presidential election. Most of our chapters were written before the final outcome was known. Federal policy can affect most of the issues discussed in this edition. And the election ultimately came down to one candidate who would more or less have continued existing federal programs and policies and another who would do something different – although what that something might be is unclear as this introduction is being written.

Where we were able to look back in time, there was more stability. History doesn't change. Our opening chapter – Daniel J.B. Mitchell on the development of the state budget enacted in June 2016 – describes a benign economic environment, basically a continuing of the expansion that took place after the Great Recession. An expansionary economic environment eases budgetary decisions by providing an inflow of tax revenue. However, Governor Jerry Brown was (and is) concerned about longer-term budget matters. One concern is the ability of the budget to withstand another economic downturn. The other concern involves two legacy infrastructure projects, a high-speed rail that is currently underway but whose completion is uncertain, and a water project that has yet even to be authorized. It is hard within the context of a one-year budget cycle to deal with the longer term.

We tend to think of public programs as budgetary, i.e., governmental, items. But there is a large nonprofit sector that undertakes programs – sometimes with government financing and sometimes using its own resources. In the second chapter, Helmut K. Anheier and David B. Howard describe the development of nonprofit foundations in the Los Angeles area. Before the Great Recession, the authors find these entities to have been cautious in their initiatives. Afterward, they began to develop a “coalition model” to increase their impact.

Our third chapter, by Robert Kleinhenz and Christopher Thornberg of Beacon Economics, looks at the economic outlook for California in 2017. Prior to the election, the outlook benefited from the same benign trend that characterized state budgeting (in Chapter 1). California draws economic strength from its tech sector. But manufacturing has been weak – an issue exposed nationally in the election campaign. The state – with its seaports and airports – has a considerable “logistics” sector linked to international trade. Thus, what may happen at the federal level in 2017 and beyond could have an important impact within the state.

Chapter 4 by Axel Sarkissian examines California's rail network. Folks in the Bay Area, Sacramento, Los Angeles, and San Diego may think of rail as primarily a local transit service. But in fact, there is an intercity passenger rail network in California. And, of course, there is the planned high-speed rail mentioned earlier whose eventual fate is unclear. Further development of the state's rail network would require significant investment in infrastructure and rolling stock.



When Matthew P. Drennan considers the history of Los Angeles' urban planning and development policy in Chapter 5, he finds notable deficiencies. Zoning and other policies have exacerbated external trends such as de-industrialization. He suggests the City focus first on efficient provision of basic services (public safety, trash collection, etc.) The barriers erected that hinder development should be removed. And the overuse of tax incentives to bid for particular employers needs to end.

There is much talk about "disruptive" new technologies that challenge older industries. In Chapter 6, Brian Nguyen, Kiana Taheri, and Blake Valenta take up policy in Los Angeles toward home-sharing services such as Airbnb, which compete with traditional hotels. There are questions of entrepreneurs running *de facto* hotels in areas not zoned for such services and of the failure of those providing rentals to pay the taxes that hotels do. Part of the solution is obtaining data from home-sharing services on those providing rentals and requiring the services to collect the appropriate taxes.

The outlook for health insurance in California – particularly the elements developed under the Affordable Care Act ("Obamacare") – is the subject of Chapter 7 by Parul Baweja, Uyen Dinh Chu, Chrissy Chung, Danielle Ogez, and Andrea Truong. With the election of President Trump – who campaigned on repealing and replacing Obamacare – the outlook is especially uncertain. After the election, but before taking office, the president-elect indicated that some parts of Obamacare might be retained. For California, an important issue is the lack of insurance of undocumented persons, who then rely on expensive emergency rooms for medical care. Of course, undocumented individuals were also the target of the Trump campaign. So, whether California will be able to undertake the kind of health insurance expansion the authors suggest is highly uncertain.

California had an unpleasant history of discrimination against Asian-origin individuals, culminating in the internment of persons of Japanese background during World War II. Daniel J.B. Mitchell, in Chapter 8, notes an aftershock of that episode that took place in Los Angeles County involving a government official who traditionally had remained in the background. But Thomas Noguchi, an immigrant from Japan who became LA County coroner in the early 1960s, was an exception. He turned the coroner's post into a highly-visible position, so visible that he was nearly pushed out of the job. Once the Japanese community in LA (which had remained largely silent after World War II) became engaged in his defense, the Noguchi story had a surprise ending.

Our final chapter by Stanley M. Paul also deals with immigrants. He looks at the case of an undocumented individual who wanted, despite his lack of official status, to become a lawyer in California. The issue was complicated by the fact that lawyers are officially licensed at the state level. Yet one candidate, Sergio C. Garcia – who had passed the bar exam – surmounted the obstacle. Others, in California and elsewhere, have since done the same. And one, as described by Paul, did so posthumously.

As noted at the outset, the outlook for California policy and economic development is not independent of national events. Future editions of *California Policy Options* will deal with the uncertain future of the state.

#### **Daniel J.B. Mitchell**

Professor Emeritus, UCLA Anderson Graduate School of Management  
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# **CHAPTER 1**

## **Not if He Can Help It: Enacting the 2016-2017 California State Budget**

**Daniel J.B. Mitchell**

Professor-Emeritus, UCLA Anderson School of Management  
and UCLA Luskin School of Public Affairs



*"Is it bye-bye, Jerry? Not if I can help it."\**

Governor Jerry Brown on avoiding the budget crisis-related  
fates of his predecessors<sup>1</sup>

The most important document any legislative body enacts is the budget. Budgets express priorities. They express values. They influence economic behavior. On the other hand, they are embedded in the larger political process that continues from one period to the next. So anything a legislature does in a particular fiscal year can be undone by some future legislature. It's hard to ensure a legacy, fiscal or otherwise.

Jerry Brown is unique in California history in having been elected to the governorship four times.<sup>2</sup> When he was first elected in 1976, there were no term limits. Nonetheless, he ran only twice for governor in his first iteration and, in his second term, he finished in the midst of a major budget crisis that he left to his successor to resolve. At the end of his first eight years, while not seeking a third term as governor, he did run for the U.S. Senate. And he lost (to San Diego Mayor Pete Wilson) in 1982.

So what would Brown's legacy have been had his career ended at that point? Not so good. He was remembered at that point for his budget crisis as he was leaving office. Longer term, he was remembered for his New Age sayings leading to the phrase "Governor Moonbeam," and for being the opposite of his dad, former Governor Pat Brown. Pat Brown is nowadays seen as a great builder of infrastructure and enhancer of higher education. It's largely forgotten that he, like his son, left a budget crisis to his successor (Ronald Reagan).

Much of what Jerry Brown has done in his second iteration as governor since his election in 2010 to a third term and in 2014 to a fourth term, has been to try to revise and reverse his previous reputation. Now he wants to be seen as the repairer of an inherited budget crisis left to him by Arnold Schwarzenegger. He wants to leave a budget process in place that will avoid a new crisis. He wants to be seen as a builder of a high-speed rail system and of a great water project involving twin tunnels in the Bay Delta area. He wants to be seen as an environmentalist, particularly with regard to reducing greenhouse gas emissions. But in doing all that, Jerry Brown wants his second iteration to be viewed as somehow consistent with his earlier

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\* This chapter takes the budget story up through July 2016. Later information is not included. Apart from official documents, much of this chapter is drawn from news media accounts. Such accounts are mainly referenced in the cases of direct quotes. Dates of references are those contained in the web versions, not necessarily the date they appeared in print versions.

<sup>1</sup> Governor Jerry Brown commenting at his May Revise news conference, May 13, 2016, on wanting to avoid the fates of former Governors Davis and Schwarzenegger when they had budget crises: <https://www.youtube.com/watch?v=Qj7v-hyht6Q>.

<sup>2</sup> Governor Earl Warren, first elected in 1942, holds the record for *consecutive* elections. He was elected three times although his third term was interrupted when he was appointed as chief justice of the U.S. Supreme Court.

iteration. In that context, this chapter provides a narrative for the development and enactment of the 2016-17 budget. For Jerry Brown, budgeting is not a routine function; it is a matter of legacy.

### **Understanding the State Budget**

*“I love the legislature, but I don’t want to entrust you with too much power...”*

Governor Jerry Brown<sup>3</sup>

In order to examine the making of the budget for fiscal year 2016-17, it’s important to understand budgetary processes, budgetary language and its pitfalls, and budgetary accounting methodology. The budget is produced through an interaction between the governor and legislature, mainly through a process by which the governor proposes and the legislature modifies. The process unfolds, sometimes with tensions over who has the major role – governor or legislature. But tensions tend to recede in good times.

### **Budgetary Institutions**

As do other state and local entities around the country, California has a General Fund – essentially the operating budget of the state. The General Fund is the source of money for education, for various social welfare programs, for prisons, and for a host of administrative and miscellaneous functions. Roughly seven out of 10 state dollars are disbursed from the General Fund. Usually, references to “the budget” refer to the General Fund.

But there are literally hundreds of special funds outside the General Fund. Typically, these special funds were set up to carry out some specific function. For example, the gasoline tax and other motor vehicle fees are earmarked for funding road repairs, road construction, and other transportation-related activities. Most people have some sense that they pay a gasoline tax at the pump that is supposed to be going toward transportation infrastructure. But few would be aware of the Fingerprint Fees Account, the Leaking Underground Storage Tank Cost Recovery Fund, the Barbering and Cosmetology Contingent Fund, the Northern California Veterans Cemetery Perpetual Maintenance Fund, or the California Collegiate License Plate Fund. Those are but a few of the many special funds outside the field of transportation.

You can think of the General Fund as the state’s household checking account. At any moment in time, money is flowing into the General Fund, mainly from taxes. And money is flowing out to cover state expenses. Some of those expenses represent activities directly provided by state agencies. Some expenses

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<sup>3</sup>David Siders, “Brown signs renewable energy bill,” Capitol Alert blog of *Sacramento Bee*, October 7, 2015. Available at <http://www.sacbee.com/news/politics-government/capitol-alert/article38089830.html>.

fund activities carried out at a lower level. They are transfers sent to local governments, especially school districts. The state's plan for the General Fund is an annual affair with a fiscal year beginning each July 1. In contrast, the special funds tend to be ongoing activities.

By state constitutional mandate, the governor makes a proposal for the next year's budget each January. By practice, the governor revises that proposal – the May Revise – in mid-May to take account of recent data on tax revenues and expenditures, forecasts of the economy, and political considerations that have arisen. The legislature must enact a budget by June 15 under the state constitution. Once the budget is received by the governor, he – there has yet to be a she in California – can veto it whole (very rare), or modify it via line-item vetoes, or just sign it “as is” (also rare). Line-item vetoes can cut particular expenditures. But the governor can't add expenditures beyond what the legislature has provided. And the entire process is supposed to be completed by the July 1 start of the new fiscal year.

### **Borrowing and Cash Management**

As with a checking account, at any moment in time, there can be a balance of dollars sitting in the “bank.” But here is where the analogy with a standard household checking account breaks down. For most households, the balance in their checking accounts – unless they have overdraft privileges – must be positive and must cover any outstanding checks that arrive. If not, the checks will bounce. In contrast, there can be times where the General Fund's balance is zero and money has to be borrowed to cover expenses.

In effect, overdrafts are not uncommon, particularly on a seasonal basis. The inflow of taxes is not evenly spread out across any twelve month period. Personal income taxes are due for most taxpayers in April, although some personal income tax revenue comes in every month through withholding. Sales taxes reflect the ups and downs of consumption patterns; Christmas sales create added revenue in November-December. But expenses of the state do not necessarily match seasonal revenue inflows. If overdrafts occur, some form of borrowing is needed.

Particularly during recessions or depressed periods of economic activity, tax revenues will be reduced. State expenses will not fall in such periods; in fact, some social welfare spending may increase. As noted, for whatever reason, when there is insufficient money in the General Fund, there needs to be borrowing to cover the costs. Problems arise because under the state constitution, external borrowing – *other than short term* – is not supposed to cover operating costs. External longer-term borrowing is supposed to be for long-lived infrastructure.

Because there are special funds outside the General Fund, balances in those funds can be tapped for internal borrowing as allowed by law. Of course, if the special funds become loaded up with IOUs from the General Fund rather than cash, their ability to carry out their earmarked functions can be impeded. To avoid or minimize such effects, the state can also borrow from the external financial markets. But – again – there are constraints.

As noted, the state constitution forbids external borrowing for operating purposes; borrowing is supposed to be for one-time infrastructure-type projects. Nevertheless, court decisions have allowed seasonal external borrowing within fiscal years. The state accomplishes such external borrowing by issuing short-term securities known as Revenue Anticipation Notes (RANs) during the fiscal year which are paid off before the year ends.

California's elected state treasurer is in charge of floating RANs as well as those longer-term securities allowed by the constitution. On rare occasions during budget crises, the state also can issue Revenue Anticipation Warrants (RAWs) which are short-term securities that cross from one fiscal year into the next. The elected state controller issues RAWs on those occasions and also handles the internal borrowing from special funds. On very rare occasions, California has found itself unable to cover expenses, even with internal and external borrowing, and has handed out Registered Warrants (essentially IOUs), to state creditors. The last time that Registered Warrants were issued was in 2009 in the aftermath of the Great Recession.

### **Budgetary Language**

Unfortunately, California-budget speak differs from federal, and in ways that are not helpful to those seeking to understand state fiscal affairs. Even with your checking account, you want to distinguish between “stocks” (how things are at a moment in time) and “flows” (changes over specified time periods). At the federal level, when the terms “surplus” or “deficit” are used, the understood meaning is simple. These are flow terms. A surplus is a situation in which more revenue is flowing into the Treasury than is flowing out in a period, usually a fiscal year. (Yes, there have been federal surpluses, most recently under President Bill Clinton.) A deficit is the opposite of a surplus, more is flowing out than coming in during a period. A balanced budget is the knife-edge situation in between surplus and deficit: the amount flowing in = the amount flowing out.

In California, and really in state and local governments more generally, what is meant by surplus, deficit, and balance is fuzzy and inconsistent. Sometimes those terms are used as they are at the federal level. But

sometimes, stocks and flows are mixed together. If the general fund has *any* money in it at the end of the fiscal year, it might be said to be in balance or even in surplus. And yet such a balanced budget or surplus budget could be headed for difficulty if the trend is outflow > inflow.

If outflow > inflow, the reserve in the General Fund will eventually be depleted. So you really want to distinguish between the reserve at a point in time (usually the end of the fiscal year), and the trend or direction in which things are moving: surplus or deficit (flows). Chronic deficits, in particular, will eventually need correction: either more revenue or reduced expenditure will be required, or both.

### **Accounting Methodology**

One way of doing the bookkeeping for the General Fund is simply to look at actual cash arriving or flowing out during the fiscal year and how much cash is in the General Fund at the start and end of the fiscal year or any period. The state controller, in fact, issues monthly cash reports for the General Fund which are readily available online. However, cash accounting is subject to accidents of timing.

For example, suppose the state is due a payment in June but, in fact, the check arrives on July 1. There really is no difference in fiscal condition whether the check had arrived on June 30 or July 1. But on a cash basis, the fiscal year ending on June 30 will be less flush because of the one-day delay. To avoid such accidents of timing, “accrual” accounting is used – both in the public and private sectors. (Corporate accounting is typically done on an accrual basis.)

Accrual accounting involves attributing receipts and expenditures to the periods they are associated with rather than when the payments actually occur. In theory, it gives a more accurate picture of the fiscal condition because accidents of timing are removed. But that’s the theory, not necessarily what happens in practice.

Cash accounting can certainly be manipulated. For example, under cash accounting – if you want to make the current fiscal year look better than it is – instead of issuing monthly paychecks for June on June 30, you could delay them until July 1. For the current year, your payroll expenses will be only 11/12ths of normal, so you will have appeared to have reduced spending even though nothing real has happened. On the other hand, accrual accounting – deciding what periods with which to link receipts and disbursements – also is open to manipulation. And it is more difficult to verify. For cash accounts, you either have the cash or you don’t. Accrued cash, on the other hand, is not necessarily actually there. Rather it is due to be there on some criterion. And the period when something is supposed to be due can be manipulated.



Accrual methodology is in fact the basis of gubernatorial budget proposals and legislative enactments. The controller does keep track of actual cash. But no reconciliation between the two approaches is provided. So mere mortals must simply accept the notion that accrual is being done “correctly.” And, changes in accrual methodology that are made from time to time mean that budget documents from one period are not necessarily consistent with budget documents from some other period.

### **A Look at the Numbers**

*“It is extremely complex. Very few people understand it. So I’m not going to try to explain it to you because I couldn’t explain it to you if I wanted to.”*

Governor Jerry Brown<sup>4</sup>

To look at the actual California budget, we start – despite the deficiencies discussed above – with an accrual presentation of the state budget’s development for the year 2016-17. We use accrual only because that is the way the governor presents his budget proposal and that is the way the legislature ultimately enacts the budget. Apart from the governor and legislature, there is another player in the process. In the early 1940s, the legislature – concerned that it did not have an independent nonpartisan source to evaluate budgets and other policies – created the Legislative Analyst’s Office (LAO). Since it is a creation of the legislature, LAO – while nonpartisan – is not exactly neutral when it comes to legislative discretion vs. gubernatorial discretion. It tends to favor proposals which provide for legislative oversight and authority and it is not keen on what it sees as too much delegation to the governor or to state agencies.

Since the governor, by constitutional mandate, must submit a budget in early January, the LAO inserts itself into the budget deliberations ahead of the governor by issuing its view of the budget outlook the previous November. However, LAO generally does not want to be in the position of adding new initiatives to state fiscal policy or removing existing ones. So its November outlook is basically a projection of what it believes would happen if existing policies on taxing and spending were continued. The budget can be expected to change as the economy develops and also based on such trends as demographics without any policy alterations. For example, if there are more children of school age, school enrollments will likely rise as will resultant spending on schools.

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<sup>4</sup>Quote number 11 in Vanessa Maravilla, “Memorable quotes from Brown's budget proposal speech,” *KCRA*, January 8, 2016. Available at <http://www.kcra.com/news/local-news/news-sacramento/memorable-quotes-from-browns-budget-proposal-speech/37320494>. Brown was referring to a tax that in a complicated way draws federal dollars for Medi-Cal (Medicaid). We discuss that tax later in this chapter.

## LAO November Outlook

Table 1 shows the LAO projection made in November 2015 in the first column on the left. The LAO expected that at the beginning of the upcoming fiscal year (July 1, 2016), there would be about \$3.2 billion in the General Fund as a reserve (a stock). There was expected to be a surplus (inflow > outflow) during the year of about \$2.1 billion which would raise the reserve in the General Fund to \$5.3 billion. In addition, the “rainy day” fund that voters voted to create in 2014 at the governor’s urging would accumulate an additional \$1.6 billion.<sup>5</sup> Total reserves, General Fund reserve + rainy day reserve would, by the end of the new fiscal year, rise to 10.3% of spending.

### Governor’s January Proposal

However, when Governor Brown made his proposal in January 2016, he provided different estimates of the starting reserve in both the General Fund and the rainy day fund. Exactly why there should have been a difference is unclear. (Second column from the left on Table 1.) Was the difference due to different forecasts of the economy, some change in accrual methodology, or other reasons? The answer isn’t evident from the basic online material. Apart from the starting reserve issue, it does appear that the governor – through the Department of Finance that produces his budget proposals – had a more conservative forecast for revenues in the then-forthcoming 2016-17 year.

On the other hand, the governor proposed more spending than the LAO’s view of what would have been spent with no change in policy. So his budget contained a General Fund deficit of about -\$2 billion rather than a surplus of that amount projected earlier by LAO. But the governor’s rainy day fund contained an offsetting surplus of about \$2 billion. So it appears that, when you look for an overview of the governor’s fiscal strategy, he was diverting monies from the regular General Fund reserve into the rainy day fund reserve. Possibly, he was making the shift because it is more difficult to tap the rainy day fund relative to the regular reserve. Possibly, it was for politically cosmetic reasons. In any event, his budget proposal net (General Fund reserve + rainy day fund) ends in June 2017 with a lower ratio of reserves to spending: 9.1% (compared to 10.3% projected by the LAO).

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<sup>5</sup>As a technical matter, the rainy day fund (Budget Stabilization Account) existed before voters – with Jerry Brown’s urging – created a mechanism to fund it in 2014 under Proposition 2. Proposition 2 provides a formula approach for diverting revenue into the rainy day fund. In addition, the legislature can directly add to it. The account had been created as a bookkeeping device as part of Governor Arnold Schwarzenegger’s plan for dealing with the budget crisis left to him after the 2003 recall election, by previous Governor Gray Davis.

## **May Revise**

By the time the May Revise rolled around, the legislature had gone through several months of hearings on budgetary matters. So the May Revise proposal of the governor was informed by both updated economic information and political information. The revenue forecast provided by the governor was a shade more conservative than in January, as was his estimate of the starting reserve in the General Fund. However, the General Fund deficit was still about -\$2 billion. It was offset by a surplus in the rainy day fund of \$3.3 billion (down from \$3.6 billion in January). The ratio of the net reserve balance to spending by the end of fiscal year 2016-17 was down to 7.7%.

## **Enacted Budget**

In terms of the macro picture, the actually-enacted budget in June 2016 differed little from the May Revise. The governor made slight changes in response to legislative pressures. But in the end there was an unusually amicable agreement. Although the governor could have exercised his line-item veto, he made no changes. Virtually all governors (including Brown in the past) have made at least minor cuts. So the budget passed by the legislature, and the budget signed soon after by the governor were identical.

## **Cash vs. Accrual**

Tables 2 and 3 provide a history of budget making during Governor Brown's second iteration. Brown's second iteration and third term began in January 2011 after his victory over Republican candidate Meg Whitman, the former CEO of eBay. Because the political year and the fiscal year are not identical, Brown's first six months in office occurred under the terms of the final budget signed by his predecessor, Arnold Schwarzenegger. Brown's first budget proposal was thus for 2011-12. He had hoped to reach agreement with legislative Republicans to place a proposition on the November 2011 ballot that would add some tax revenue, but his negotiations with them went nowhere. At the last minute – to produce a budget that was at least cosmetically “balanced” – the budget was enacted by assuming a phantom \$4 billion in extra revenue that would appear somehow.<sup>6</sup> (It wasn't specified *which* tax or taxes would produce this extra revenue.)

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<sup>6</sup>We remind the reader of the fuzzy language issue associated with state budgets. The back story is complicated. Brown had a choice between using an initiative to put the tax measure on the ballot (a petition with requisite signatures of registered voters) and doing it via the legislature – which required a two-thirds vote. He wanted to use the legislative option, which meant he would need a few Republican votes, because he thought it would look more bipartisan to voters. Voters had earlier approved a ballot proposition cutting the requirement for passing a budget from two thirds to a simple majority (but retaining two-thirds for increased taxes). To pass the budget, therefore, only a simple majority

When the following year's budget was enacted (2012-13), it included an estimate for the Phantom-4 year which, not surprisingly, was in deficit (revenue < spending); put another way, the phantom did not arrive.<sup>7</sup> But when you look up budget history documents *now* – as reflected on Table 2 – the Phantom-4 year shows a surplus. This type of retroactive revision of history illustrates the problem inherent in accrual accounting. What accounted for the switch from deficit to surplus? Who knows?

Table 3 – which is on a cash basis – shows an unsurprising deficit after the fact for the Phantom-4 year when imaginary revenue was assumed. So on an accrual basis in a year when an imaginary \$4 billion was assumed to pass a budget, the deficit eventually disappeared from the historical record. But cash is cash and the expected consequence – a deficit – remains. Perhaps there is a lesson about accrual versus cash accounting here. If you want to understand what is going on, the former is better in theory; the latter is better in practice.

The problem of the discrepancy between cash and accrual continues thereafter. Readers will note on (accrual) Table 2 there is a gap in 2013-14 between figures reported as an historical time series and figures on another document, both on the official website at this writing. Unfortunately, 2013-14 is the first year in which the full impact of a tax-raising initiative – Prop 30 endorsed by Governor Brown – can be seen. And the discrepancies between Tables 2 and 3 continue. Total reserves seem to be lower using cash accounting than accrual. But without a clear reconciliation table explaining the differences, it's hard to know what the true situation is.

California, circa 2000, deserved praise for having put its basic budget documents available on the web. At the time, that level of transparency was an achievement, perhaps a reflection of the state's high-tech industry. But years later, just putting what used to be paper format documents on the web is routine for state and local governments around the country. The next step should be to make interpretation of official budget documents easy. Unfortunately, in that area, California hasn't advanced since 2000.

### **Avoiding a Future Crisis**

Can we at least say that California's fiscal situation is notably better now than it was back in 2010 when Governor Brown was elected to the beginning of his second iteration? Even if the precise condition of the reserves available to the General Fund is somewhat obscure, there are more resources available to deal with

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was needed and it had to look "balanced" on paper. The result was the assumption of a phantom \$4 billion in revenue above what had been forecast for the various taxes the state collects. As a result, the phantom \$4 billion was not allocated to any particular tax or taxes but was assumed to come as a surprise within some tax somehow.

<sup>7</sup><http://www.ebudget.ca.gov/2012-13-EN/pdf/Enacted/BudgetSummary/SummaryCharts.pdf>.

a downturn than there were back then. Resources available go beyond what is officially in reserve accounts. As noted previously, apart from the General Fund, the state has other special funds earmarked for particular functions. And as also noted earlier, in the case of a pinch, the state controller can move cash – in the form of an internal loan – from those funds to the General Fund.

The monthly reports of the state controller show the total in those special funds minus what borrowings have already been made by the General Fund, a sum known as Unused Borrowable Reserves. Figure 1 compares crisis year 2009-10 with now completed 2015-16 and with projections for 2016-17. In the crisis year, such resources fell to below 5% of annual spending in some months. Indeed, as the figure shows, July 2009 – the point in time when IOUs began to be distributed in lieu of actual payments – was such a month. In contrast, the *peak* month of the 2009-10 fiscal year in terms of Unused Borrowable Reserves relative to annual pending was below the *troughs* of 2015-16 and the projected troughs of 2016-17. So the state clearly has more of a cash cushion now than it did back then.

In short, the fiscal condition of the state is clearly better, due to the economic recovery since the crisis year, the added tax revenue from Prop 30 of 2012, and constraints on spending. Still, reserves are a cushion, not a total insulation, from the business cycle. If there were to be a downturn, the state would have a couple of years to complete taking steps – perhaps painful steps – to reduce spending to available revenue. And as noted previously, if you drain out the special funds by taking their cash and giving them IOUs instead, you hinder the ability of those funds to carry out their designated functions. In effect, you are protecting activities of the General Fund at the expense of activities of the special funds.

At present, we finish each fiscal year with a ratio of Unused Available Reserves to spending in the 25-30% range. In crisis year 2009-10, the ending ratio was around 10%. In the peak of the late 1990s (dot-com boom), the ratio was around 15% as it was at the peak of the housing bubble/boom (2006-07). So we definitely have more resources on hand now than then. Nonetheless, California has a special vulnerability from the heavy reliance of state finance on the personal income tax, a reliance that has risen over time.

The personal income tax is progressive and thus is heavily dependent on tax liabilities of high-income Californians whose taxable incomes reflect capital gains and losses in financial markets. The top one percent of taxpayers paid 48% of income tax revenues in 2014; the top fifth paid 90 percent.<sup>8</sup> About two thirds of the revenue projected to go into the General Fund in 2016-17 comes from the personal income tax. If we combine General Fund revenues with those going into the special funds, the proportion is smaller. But it's

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<sup>8</sup>Jim Miller, "Almost half of California 2014 income taxes paid by top 1 percent," Capitol Alert of *Sacramento Bee*, April 27, 2016. Available at <http://www.sacbee.com/news/politics-government/capitol-alert/article74271532.html>.

still about half. Under Jerry Brown, resources to deal with downturns have increased but so has state vulnerability to downturns.<sup>9</sup>

### How We Got There

*“Jerry has always been a reflective, thoughtful guy. I always thought when we were in school together that he would be a philosopher.”*

Father John Coleman commenting on  
Brown’s signing a right-to-die bill<sup>10</sup>

We have traced the numerical development of the 2016-17 budget. But what was the political background? How did we get to the eventual numbers? Although we think of each year’s budget as a thing in itself, the budget is in fact an evolving story. Issues left over from one fiscal year are carried into the next. Even enacted budgets are not “final.” Without any legislative change, economic trends and their relation to revenues generated may evolve differently from budgetary assumptions and lead to different outcomes. Similarly, expenditures in many programs depend on factors that may develop differently from what was assumed.

Apart from external influences such as the economy, the legislature itself may make budgetary modifications in the course of a year. In some cases, voters may have an influence on the budget through ballot propositions. While the most dramatic mid-course changes in the budget tend to occur during fiscal crises, no budget is absolutely fixed, even in good times. Good times, however, make for a calmer fiscal atmosphere than do hard times with their resulting conflicts over a diminished pie to divide. Fiscal 2015-16 began with a clear indication that a crisis any time soon was very unlikely, so there was the expected sense of calm compared to the atmosphere of earlier years. Indeed, State Controller Betty Yee announced that there was sufficient internal cash on hand to meet all seasonal ups and downs in revenue and spending during the year. No short-term external borrowing via RANs was expected.

### Follow on to the 2015-16 Budget

A variety of issues remained on the agenda after the previous 2015-16 budget was put in place. There were the two legacy infrastructure projects of Governor Brown: the high-speed rail train and the water tunnels. Opposition to, or skepticism about, the two projects was not confined to GOP legislators. Some Democrats

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<sup>9</sup>Reliance on the personal income tax was increased by the governor’s Prop 30. It will be further increased if voters approve the extension of the temporary income tax component of Prop 30 in the November 2016 election.

<sup>10</sup>Kevin Fagan, “Jerry Brown’s thoughts turn to end-of-life issues,” *San Francisco Chronicle*, October 5, 2015. Available at <http://www.sfchronicle.com/news/article/Jerry-Brown-s-thoughts-turn-to-end-of-life-6552385.php>.

were also not sympathetic. Looking ahead, there was growing interest during the fiscal year about what propositions might wind up on the November 2016 ballot. Presidential politics increasingly received public attention as the fiscal year progressed, particularly as the June 2016 primary approached.<sup>11</sup> From time to time, there was speculation that Governor Brown in his last term – and given his interest in the presidency earlier in his long career – might enter the Democratic race. Brown had made his disdain for eventual Republican candidate Donald Trump known early on, although he said little about it until after the primary.<sup>12</sup> But Brown never indicated any personal interest in running himself.

However, with Governor Brown termed out in California, state-level gubernatorial politics for 2018 were already in evidence. One candidate, Lieutenant Governor Gavin Newsom, was already in the contest. State Treasurer John Chiang would be added as a candidate as the fiscal year progressed. And there were other possible names as well, such as former Los Angeles mayor Antonio Villaraigosa.<sup>13</sup> Newsom in the past, it might be noted, had expressed opposition to Brown's high-speed rail. He began taking positions on other matters as well, favoring strong gun control and the legalization of marijuana.

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<sup>11</sup>As the year progressed and both the Democratic and Republican races took unexpected turns, it appeared for a time that the California primary – even though it came late in the political contests – might be crucial in determining the nominee of one or both parties. Vermont Senator Bernie Sanders mounted a surprisingly strong challenge to Hillary Clinton on the Democratic side. And Donald Trump emerged to be the leading Republican candidate out of a herd of GOP contenders. But in neither case did the California primary turn out to be decisive. Both Clinton and Trump had essentially locked up their nominations by June 2016. Brown stayed out of presidential politics until shortly before the June 2016 California primary at which point he endorsed Hillary Clinton over rival Sanders. As might be expected, Brown did not have anything positive to say about GOP candidate Trump, although he said little about him through the primary. At the Democratic convention in July, he attacked Trump on the global warming issue: *"Trump says global warming is a hoax. I say Trump is a fraud. Trump says there's no drought in California, I say Trump lies. So it's not surprising that Trump chose as his running mate a man who denies that there's such a thing as evolution."* See Ted Johnson, "Jerry Brown Calls Donald Trump a 'Fraud,'" *Variety*, July 27, 2016. Available at <http://variety.com/2016/biz/news/jerry-brown-donald-trump-fraud-democratic-national-convention-1201825025/>.

<sup>12</sup>There was another California element in the presidential race. When Trump became a candidate, he was replaced on the "Celebrity Apprentice" TV show he had been hosting by Arnold Schwarzenegger who had resumed his acting career after his two terms as California governor.

<sup>13</sup>In early polling, the California Field Poll included Newsom, Villaraigosa, Chiang, current LA mayor Eric Garcetti, wealthy environmentalist Tom Steyer, former state controller Steve Westly – all Democrats – as well as two Republicans: Fresno mayor Ashley Swearengen and San Diego mayor Kevin Falconer (who later explicitly said he would not run). Available at <http://www.field.com/fieldpollonline/subscribers/RIs2520.pdf>. Even a rumor of possible candidacy immediately brings public scrutiny. Westly, who was a past candidate for the Democratic nomination for governor, was suddenly the subject of a *Wall Street Journal* article about his business association with a man charged with domestic abuse. Jeff Elder, "How Politician Steve Westly Helped RadiumOne CEO Amid Scandal," *Wall Street Journal*, September 9, 2015. Available at <http://blogs.wsj.com/digits/2015/09/09/how-politician-steve-westly-helped-radiumone-ceo-amid-scandal/>.



Rainy-Day Fund Issues: One legacy item that Governor Brown already had in place was his rainy-day fund under Prop 2 of 2014.<sup>14</sup> Part of the deal through which that proposition got to the ballot was inclusion of a limit on local school district reserves, ostensibly on the rationale that if the state had a big enough reserve, local districts wouldn't need large cautionary balances of their own. Teachers' unions pushed for the local limit on reserves to prevent districts from tucking away money that might otherwise be used for salaries. There was an attempt in the legislature by the districts during summer 2015 to ease the local limit, but the effort ultimately failed. Nonetheless, the issue continues to simmer.

Public Pensions: Another political failure was a proposed initiative to restrict public pension systems. A group led by a former city councilmember from San Diego and a former mayor of San Jose has periodically promoted such an initiative, but it never has raised the money that would be needed for a campaign. After a flurry of interest, the effort ended, at least with regard to the November 2016 ballot. Since public pensions continue to be underfunded, the issue remains. But unless some wealthy individuals want to fund a campaign (the issue is popular in conservative circles), it would be difficult to mount a successful effort.

Governor Brown – who earlier had his own plan for pensions enacted – continued to pressure the state's plans (CalPERS, CalSTRS, and the University of California {UC} pension system) to deal with underfunding.<sup>15</sup> He has also pushed various state labor unions to raise employee contributions to retiree health care.<sup>16</sup> However, although the focus in the political sphere has been on public employees' retirement costs, there is

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<sup>14</sup>Brown had only modest Republican opposition from Neel Kashkari, an obscure former U.S. Treasury official, in the 2014 gubernatorial election. Instead of running TV ads directly in support of his campaign, Brown ran ads for Prop 1 (a water bond) and Prop 2, the rainy-day fund. In the ads, Brown appeared and urged voters to support the two propositions. He never directly said to vote for him, too. Kashkari, after losing the election, was appointed president of the Federal Reserve Bank of Minneapolis.

<sup>15</sup>CalPERS covers most state employees (except the University of California) and many local employees. It has been engaged in litigation against the bankrupt City of San Bernardino which skipped some required payments into the system. CalSTRS covers school teachers. The University of California was originally exempted from the governor's legislation but was included *de facto* later in a deal with the Regents that was implemented in the spring of 2016. The UC deal was controversial and at one point a legislative committee threatened to override it. All three state systems may need to reduce assumed rates of return on their portfolios which would increase their calculated rates of underfunding. In recent years, the systems have assumed long-term annual rates of return of 7.25% – 7.50%. The governor thinks 6.5% would be more realistic. Statements of the administrators of the UC plan suggest agreement with the governor about the estimate. One concern has been a tendency – for political reasons – to pressure public pensions to divest from disfavored industries. The latest example was a bill requiring divestment from coal – due to environmental effects – passed in September 2015. Note that the state has no coal industry – but *does* have a significant oil industry. Both coal and oil are fossil fuels and both have adverse environmental effects when burned. It is not always the case that politically disfavored industries are bad investments or that the legislature can make such distinctions.

<sup>16</sup>A contract with an engineers' union reached in August 2015 provided for such a contribution. The Brown administration thus signaled it would push for similar terms with other unions. However, members of a union of state scientists rejected such a contract in early October.

a much larger long-term issue of the aging population in the state (and in the U.S.) as the baby boomers retire. State programs of social service will be affected by the demographics of aging, but there has been little advance planning. Yet the aging population creates a kind of implicit unfunded liability for the state, even though such demographic liabilities don't necessarily show up in official bookkeeping the way public pension liabilities do.<sup>17</sup>

There continued to be study, but no final enacted version, of a plan to create a pension benefit for *private-sector* workers whose employers didn't provide one. The basic idea is to create a kind of state-sponsored, tax-favored IRA-type plan ("Secure Choice") that employees themselves would finance at no risk and no cost to the state. Several states have such plans under consideration. A key element is that eligible employees would be automatically enrolled in the plan for payroll deductions/savings contributions. They could opt out, so the plan would be voluntary. But behavioral research suggests that if making contributions is the default status, most people won't opt out.<sup>18</sup> At least some of the motivation behind the plan, which remained in development and consideration throughout the budget cycle, is to lessen public concern about public pensions and to focus instead on the idea that all workers should have a retirement benefit program.

Education: Although education is the biggest single item in the state budget, school districts also rely on federal funding. There has been a history of the state being out of compliance with federal testing mandates for students, but ultimately obtaining waivers for its deviations. In the latest version of this process, the legislature scrapped its high school exit exam requirement in August 2015, allowing those students who failed the test to obtain their diplomas anyway. It remained unclear what type of exam would be the future replacement for the abandoned test.<sup>19</sup> Given the past history of federal acquiescence, the legislature may well have assumed that in the end there would be no cut in federal funding.<sup>20</sup> But the reality is that

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<sup>17</sup>Public Policy Institute of California, "Planning for California's Growing Senior Population," August 2015. Available at [http://www.ppic.org/main/publication\\_quick.asp?i=1156](http://www.ppic.org/main/publication_quick.asp?i=1156).

<sup>18</sup>See <http://www.treasurer.ca.gov/scib/>. The initial impetus for the plan came as a result of legislation in 2012. See also Anek Belbase, Alicia H. Munnell, Nari Rhee, and Geoffrey T. Sanzenbacher, "State Savings Initiatives: Lessons from California and Connecticut," Boston College: Center for Retirement Research, March 2016. Available at [http://crr.bc.edu/wp-content/uploads/2016/03/IB\\_16-5.pdf](http://crr.bc.edu/wp-content/uploads/2016/03/IB_16-5.pdf).

<sup>19</sup>The state Department of Education for a time removed from its website historical data on test scores. After an outcry, it restored the information.

<sup>20</sup>The resignation announcement of U.S. Secretary of Education Arne Duncan – an advocate of testing – came later in the year (in early October 2015). That resignation may turn out to ease some of the conflict between the state and the federal government on educational performance measures.

California students tend to score below the national average in standardized tests, even after demographic adjustment.<sup>21</sup>

At the higher education level, there remained tension between the legislature and UC over out-of-state admissions which produce added revenue for the university through tuition surcharges. The legislature offered UC an extra \$25 million to enroll 5,000 more in-state students but the added enrollment didn't happen in the 2015-16 academic year. By UC's calculation, the offer – effectively \$5,000 per extra student – doesn't cover the marginal cost. Nonetheless, the legislature left the offer on the table for the following year; eventually the university agreed to expand admissions.

Initiatives: Although under Prop 13 of 1978, a two-thirds vote of the legislature is required to raise state taxes, fees (user charges) can be raised by a simple majority.<sup>22</sup> The fee for filing initiatives had been \$200 for decades and, as a result, many proposed propositions were filed by citizens without a prayer of collecting the needed signatures. Some of these filings were done with the hope of generating publicity for various causes. Some were filed in the false hope that other citizens would somehow spontaneously provide the signatures. However, after the filing of an initiative that would have made it legal to murder homosexuals, there was public outrage about the process. As a consequence, the legislature enacted a fee increase to \$2,000. The purpose was not to raise more revenue but rather to discourage frivolous or hateful filings.<sup>23</sup>

Taxes: One initiative that was filed in August 2015 – but that never got to the ballot – would have imposed a property tax surcharge on properties valued above \$3 million with the funds used for various anti-poverty programs. Of course, the vast majority of homes – even with the high values that characterize much of urban California – would not be affected.<sup>24</sup> Nonetheless, anything that touches on property taxes incurs the wrath of Prop 13 advocates. In the end, the effort was dropped.

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<sup>21</sup>Comparative state scores on the tests of the National Assessment of Educational Progress can be found at <http://nces.ed.gov/nationsreportcard/states/>. See also Urban Institute, "How do states really stack up on the 2015 NAEP?," October 28, 2015. Available at <http://www.urban.org/urban-wire/how-do-states-really-stack-2015-naep>.

<sup>22</sup>The distinction between fees and taxes can be fuzzy in some cases. Nonetheless, in 1996, voters enacted Prop 218 which tightened the definition of fees to prevent *de facto* tax increases.

<sup>23</sup>When an initiative is filed, the Legislative Analyst's Office must analyze the proposal and produce a statement of budgetary impact. The attorney general must come up with a description and title. The estimated cost of these requirements was put at \$8,000 per filing, but the legislature was reluctant to raise the fee that high.

<sup>24</sup>Note that many properties are not residences but are commercial. The proposal would also have covered rental properties with exemptions for lower-value properties. The Legislative Analyst's Office (LAO) estimated the proposed surcharge would have raised \$6-\$7 billion annually. See <http://www.lao.ca.gov/BallotAnalysis/Initiative/2015-043>.

But other ideas for raising tax revenue persisted. A poll indicated general public support for an increase in tobacco taxes.<sup>25</sup> (Most voters are not smokers.) And the prospect that Governor Brown's Prop 30 temporary income and sales taxes (enacted in 2012) would be expiring, led to proposals to extend their life – or at least the life of the income tax component.<sup>26</sup> Brown, who promised the voters that the Prop 30 taxes were to be temporary, was not a supporter of an extension. However, he was not an overt opponent, either, and just took a neutral position on what ultimately was slated to go on the November 2016 ballot, a proposal to extend just the income tax component to 2030.<sup>27</sup> (The sales tax component was not to be extended.)

Cap-and-Trade: Cap-and-trade is a state-run program under which the state auctions off a limited number of permits to emit that emitters must purchase. In principle, the overall level of state emissions will drop as the number of permits declines. Governor Brown was not neutral about cap-and-trade revenues since these were an important element in the financing of his high-speed rail project on which construction has begun, even in the absence of a full funding plan.<sup>28</sup> Later in the fiscal year, cap-and-trade posed two important issues for the governor in terms of revenue actually collected and the long-term legal authorization for the program. (The revenue from permit auctions fell below expectations although substantial unspent funds remained from earlier auctions.) There was persistent unhappiness among some in the legislature (not just the Republicans) about the program's support for high-speed rail. The Legislative Analyst's Office tended to approach the issue gingerly. However, it issued a report in September 2015 that grumbled about the lack of a mechanism for establishing clear and objective priorities for cap-and-trade spending.<sup>29</sup>

Transportation: The thing about cap-and-trade is that although it has tax-like properties, it isn't technically a tax. At least, that is the view of the governor and the Democratic majority in the legislature. (That issue is the subject of litigation.) Brown advocated a combination of motor vehicle fees, gas tax hikes, and cap-and-trade revenue for repair of transportation infrastructure. But to put such a plan on the ballot through the legislature, or to enact it directly legislatively, he needed a two-thirds vote of the legislature. Reaching that margin would have required some Republican votes. Although he made some concessions to GOP

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<sup>25</sup>Public Policy Institute of California, "Californians & their government," September 2016. Available at [http://www.ppica.org/content/pubs/survey/S\\_915MBS.pdf](http://www.ppica.org/content/pubs/survey/S_915MBS.pdf).

<sup>26</sup>The sales tax component under Prop 30 expires at the end of calendar 2016. The income tax component expires at the end of calendar 2018.

<sup>27</sup>The extension was estimated to produce an added \$5-\$11 billion per year in state revenue in the ballot statement produced by the Legislative Analyst's Office.

<sup>28</sup>Chinese firms have expressed some interest in the construction and financing of the project. (China has built high-speed rail projects domestically.) But whether they will be involved is uncertain. Other international firms – such as Siemens – have also expressed tentative interest.

<sup>29</sup>Legislative Analyst's Office, "Framework for Cap-and-Trade Investment Plan Needs Further Development," September 2015. Available at <http://www.lao.ca.gov/publications/report/3298>.

legislators, the needed votes were not to be had. Without those votes, the governor's plan died. (It could be revived at some future date.)

Health Care: Also at risk of dying for lack of sufficient support was a complex plan that adds federal revenue to state health plans. Basically, the federal government matches revenue raised by a state tax on health providers. If done artfully, the state tax can reimburse providers for the cost of the tax and still leave federal matching money over for the state. Put another way, if the state can channel sufficient revenue back to providers, they will be held harmless. But the state will get a net subsidy from the feds.

However, "artfully" is the key word here. The state had a version of the tax/reimbursement plan in place, but the federal authorities found it wanting for technical reasons. To replace the old plan, there had to be a new tax design that met federal standards. And even though the plan was a plus for the state, a two-thirds vote (and thus Republican support) was needed since the plan involved a tax. It appeared by mid-September 2015 that a deal couldn't be reached. (None was reached for the next half year until an accord was negotiated with health providers; at that point the tax was passed by the legislature.)

Bond-Related Projects: September also saw another complication for Governor Brown's legacy, his water tunnels definitely and high-speed rail possibly. An initiative was filed – and later obtained sufficient signatures for the November 2016 ballot – that would require voter approval for specific bond-financed projects if they were to be operated by a state agency. Projects that have commercial elements, i.e., projects that generate revenues from users, create resources that can be used to pay off the bonds that the agencies issue. But project sponsors would be unable to issue such bonds without project-by-project approval. What voters will do with this initiative or, if they pass it, what they will do with specific projects on which they are asked to opine is unknown at this writing.<sup>30</sup>

Brown's water tunnel project, if it had to come to a direct vote, might benefit from California's ongoing drought, which has led to local water cutbacks, water rate (price) increases, and restrictions on water uses. But exactly how the tunnels relate to drought issues has never been clear in the public mind. And even if the tunnel project were to be sold to voters as a drought remedy, the ballot proposition would add a hurdle to actual construction that wasn't present before. Because the rail project's future funding mechanisms are

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<sup>30</sup>If the initiative were passed by voters, there would undoubtedly be issues about state agency efficiency in running infrastructure projects. The replacement span of the Bay Bridge would likely be raised as a model of state deficiencies in project administration. The new bridge has been plagued by falsified reports, defective components, and improper construction causing increased costs and potentially shortening its life.

uncertain at this point, additional bond financing might be an option. But if the proposition passed, the rail project – like the tunnels – would face an additional hurdle.<sup>31</sup>

Redevelopment: The legislature ultimately did enact what might be viewed as a partial cleanup of a problem created at the local government level in the aftermath of the Great Recession’s budget crisis. For many years, local governments had the authority to create redevelopment agencies which were supposed to revitalize blighted areas. (How well the agencies did so is a matter of controversy.) The redevelopment agencies worked in part through incremental tax financing. If they succeeded in revitalizing an area, its property values would rise (and thus property taxes would rise). The tax increment so generated could be used to pay off bonds that provided the funding for whatever redevelopment project was involved. Over time, however, the growing share of property taxes taken by the agencies was seen by some folks at the state level as a “diversion” from other local finance, such as funds for schools.<sup>32</sup>

Redevelopment, originally a purely local affair, became intertwined with state finance when Prop 98 was enacted in 1988. Prop 98 requires the state to fund K-14 school and community college districts according to a formula that takes into account both state revenue and local property tax. To the extent that property taxes were “diverted” from schools to redevelopment, the state would thus have to make up that amount out of its general fund. Governor Brown, as part of his effort to deal with the budget crisis he inherited from his predecessor, proposed to abolish redevelopment agencies – and thus indirectly save money for the general fund. The redevelopment agencies fought the proposal and eventually a tentative deal was reached which preserved the agencies but required them to contribute to the state budget. After the deal was enacted, the agencies challenged the arrangement in court. But the court threw out not just the forced contribution but the entire redevelopment system and the agencies were abruptly abolished. Through litigation, they had rolled the dice by challenging the forced contribution and in the end abolished themselves.

The abolition of redevelopment was a messy process, in part because there were projects that were underway and had to be completed. In addition, while the state gained due to increased property taxes going to K-14 that it didn’t have to backfill, local governments were also due some revenue that would no longer be “diverted” for redevelopment. Exactly who owed what to whom involved expensive and uncertain litigation. In September 2015, legislation was enacted to simplify the cleanup process. It also created a new,

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<sup>31</sup>There was an effort to put an initiative on the ballot in November 2016 that would have diverted high-speed rail money to “water storage” projects. However, proponents abandoned the effort.

<sup>32</sup>Note that it could be argued that the extra revenue would not have existed absent the redevelopment and thus should not be seen as a diversion.

cut-back version of redevelopment that could be used for affordable housing and other purposes, but would not involve diversion of property taxes from K-14. Put another way, the new, limited version of redevelopment would not lead to indirect impacts on the state budget.

### **Moving Towards 2016-17**

There is no absolute point in which the governor and legislature move from dealing with the aftermath of one budget year to beginning to plan for the next. But the end of September/early October tends to be a transition period. September produces a pile up of bills on the governor's desk which he can sign or veto. Some of the bills have budget implications, but many other issues are involved. For example, Brown vetoed some proposals to expand the state's Medi-Cal (Medicaid) program, citing fiscal concerns. (Nonetheless, Medi-Cal expanded in the course of 2015-16 to cover low-income undocumented children.) On the non-budget front, Brown had increasingly become an advocate of reducing greenhouse gas emissions – which he termed an “existential threat” to humanity – during his second iteration as governor.<sup>33</sup> He signed a compromise bill aimed at reducing such emissions from state electricity generation.<sup>34</sup>

Environment: A mini-scandal erupted when it was revealed that a state agency – at the governor's request – had looked at the prospects for oil and gas drilling on property he owned. But the fact that there turned out to be little chance of oil or gas production on the land tamped down the affair.<sup>35</sup> Despite the scandal, the governor made himself highly visible on the environmental stage by participating in the Paris climate conference in early December 2015; he told the experts assembled there that “*you know all the numbers and I have all the answers.*”<sup>36</sup> Generally, Californians – at least when no overt cost to them is attached to the plans – are supportive of mandating cleaner energy, subsidizing electric cars, and similar steps.<sup>37</sup> Whether they would like to pay higher taxes or higher energy prices in support of such efforts is less clear.

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<sup>33</sup>Chris Jennewein, “Governor: Climate Change Challenge Equivalent to World War II,” *Times of San Diego*, October 27, 2015. Available at <http://timesofsandiego.com/education/2015/10/27/governor-climate-change-challenge-equivalent-to-world-war-ii/>.

<sup>34</sup>The bill originally sought to reduce state petroleum use more generally and included targets for motor vehicles. But those elements were removed in the final version.

<sup>35</sup>“Gov. Jerry Brown had state workers research oil on family ranch,” *Los Angeles Times*, November 5, 2015. Available at <http://www.latimes.com/local/political/la-me-pc-brown-state-research-oil-ranch-20151105-story.html>.

<sup>36</sup>David Siders, “Jerry Brown: ‘This will be somewhat of an asymmetrical encounter,’” Capitol Alert of *Sacramento Bee*, December 9, 2015. Available at <http://www.sacbee.com/news/politics-government/capitol-alert/article48917670.html>.

<sup>37</sup>Public Policy Institute of California, “Californians & the environment,” July 2015. Available at [http://www.ppica.org/content/pubs/survey/S\\_715MBS.pdf](http://www.ppica.org/content/pubs/survey/S_715MBS.pdf).



Higher Ed: Environmental issues are not unique to the extent that there is abstract support for various policies but less support if some personal cost to implementing those policies is entailed. Californians want access to higher education institutions, but they are not keen on paying increased tuition or taxes to make it happen. The state reduced its support of higher ed institutions over a long period. A factor in this reduction is that the legislature is aware that, unlike other functions (such as prisons), if it reduces direct payments to higher ed institutions (UC, CSU, and the community colleges), they can make it up via charging more to users (students). So legislators can indirectly cause tuition to rise and yet complain about it when it happens.

One response of students and parents has been to use the lesser expensive community colleges for the first two years of post-secondary education. California has a much higher rate of undergraduate enrollment in community colleges among those attending a public institution than most other states.<sup>38</sup> Despite concerns raised by student groups about costs and capacity, the UC Regents voted in November 2015 to increase in-state enrollment by 5,000 in fall 2016 and another 5,000 the following year.

Crime: Issues such as environmental protections and accessibility of higher education are continuous. They compete with others that also pass from year to year. For example, crime rates, convictions, and penalties for crimes ultimately determine the prison population and thus prison costs. A rise in crime in the 1980s and into the 1990s led to public pressure and legislation such as the three strikes law which put more criminals in prison and for longer. Eventually, prison overcrowding led to federal court decisions requiring the state either to build substantially more capacity or release inmates. The state primarily chose the latter, moving prisoners it deemed least dangerous to local jails and, effectively, bumping some felons back into the streets, a process known as “realignment.”

California voters had a long history of voting for increased penalties and of refusing to modify three strikes. But in 2014, due to a mix of lower crime rates and the high costs of prisons, voters enacted Prop 47 which reduced penalties for some crimes. Police officials tend to believe that at least low level crime has increased as a result of realignment and Prop 47. Data on recent crime rate trends are at best ambiguous; there is a leveling out of the prior declining trend. Whether that leveling effect is connected to the inmate releases

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<sup>38</sup>Campaign for College Opportunity, “Rising Selectivity at California’s Public Universities,” November 2015, p. 33. Available at <http://collegecampaign.org/portfolio/november-2015-access-denied-rising-selectivity-at-californias-public-universities/>. See also John Aubrey Douglass, “Funding Challenges at the University of California: Balancing Quantity with Quality and the Prospect of a Significantly Revised Social Contract,” *California Journal of Politics & Policy*, 7(4)2015. Available at <http://escholarship.org/uc/item/5tb9302t.pdf>.

and Prop 47 is unclear.<sup>39</sup> Ultimately, however, what the public comes to believe is happening is what leads to political responses.

Guns: The crime issue is partially related to the issue of gun control. We don't think of gun control as a budgetary issue primarily, but any regulatory program has some fiscal impact since enforcement costs money. In the case of gun control, however, another issue of resources opened up in November 2015. Lieutenant Governor Gavin Newsom – as part of his campaign to succeed Governor Brown – pushed for an initiative on gun control which ultimately made it to the November 2016 ballot. But in doing so he came into competition with state senate leader Kevin de León who wanted to pursue a legislative approach to guns. The lieutenant governor is the titular head of the senate. So De León reduced Newsom's staff support, although his aides denied there was any connection to the competition. The issue of guns, however, in the course of the budget cycle became progressively linked to terrorism due to attacks in Paris, San Bernardino, Orlando, and elsewhere. As a result there was political space for both a legislative and ballot approach to the gun control issue.

Advance Knowledge: The various issues described above in this section were floating around as the governor's January 2016 State of the State address and his budget proposal were in preparation. But one thing didn't happen in this period which has occurred in the past. Usually, before the governor's State of the State address and budget proposal, bits and pieces of his new agenda are leaked out in advance. But such leaking did not occur in this cycle except for the unsurprising news that Brown would propose a revamped Medi-Cal tax to keep the federal match flowing.

About the only other thing that became known, and not by leaks but instead through monthly statements of the state controller, was state revenue for the first five months of the fiscal year. As it turned out, revenue was running ahead of the projections made as part of the enactment of the 2015-16 budget.<sup>40</sup> Such a result – more money flowing in than forecast – tends to lead to new spending proposals; something the governor dislikes to see encouraged.

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<sup>39</sup>Crime rate data through 2015 are available from the attorney general at <https://oag.ca.gov/sites/all/files/agweb/pdfs/cjsc/publications/candd/cd15/cd15.pdf>.

<sup>40</sup>Revenues for the sixth month of the fiscal year (December) were not available when the January budget proposal was first unveiled. But when the controller published the figures through December on January 11, 2016, revenues were still ahead of the projections made at the time that the 2015-16 budget was passed.

## Unveiling the January Proposal

*"If you don't remember anything else, just remember everything that goes up comes down."*

Governor Jerry Brown presenting his January budget proposal<sup>41</sup>

Brown's budget proposal presentation in January focused more on the risks to fiscal stability from potential downturns in the economy and financial markets than on discussion of immediate goals. The emphasis was on building up the rainy day fund and some infrastructure investments such as repairing and replacing state office buildings. After the budget was unveiled, the governor selectively avoided discussion of ballot measures that were heading towards, or had already gotten to, the November 2016 ballot. However, he did induce backers of a plan to extend Prop 30 temporary taxes – or at least the income tax portion thereof – to modify an element of their proposal he termed a "fatal flaw" that would have circumvented the formula for adding to the rainy day reserve.<sup>42</sup> He also continued to push for his water tunnels, despite environmentalist opposition, raising the specter that at some point – absent the tunnels – the Silicon Valley would be "cut off" from water access.<sup>43</sup>

Once the governor makes his proposals for the budget, responsibility shifts to the legislature which enters into a period of hearings and alternative proposals. The Legislative Analyst's Office assists in the process by providing background materials on particular policies for relevant legislative committees. However, the governor gets a second chance to reinforce his fiscal themes through his State of the State address. And again he hit a cautionary note: *"You are not going to hear me talk today about new programs. Rather I am going to focus on how we pay for the commitments we have already made."*<sup>44</sup>

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<sup>41</sup>Alex Matthews, "Words of gloom accompany Brown's budget," *Capitol Weekly*, January 7, 2016. Available at <http://capitolweekly.net/words-gloom-accompany-browns-budget/>.

<sup>42</sup>David Siders, "Tax increase backers add reserve, per Jerry Brown demand," *Capitol Alert of Sacramento Bee*, January 12, 2016. Available at <http://www.sacbee.com/news/politics-government/capitol-alert/article54290850.html>.

<sup>43</sup>Christine Mai-Duc, "Brown defends Delta tunnels as he rolls out tweaks to water plan," *Los Angeles Times*, January 14, 2016. Available at <http://www.latimes.com/politics/la-pol-sac-jerry-brown-water-plan-delta-tunnels-20160114-story.html>. Environmentalists managed to get the federal government involved in an investigation of whether the state had improperly used federal funds for tunnel planning. See Carolyn Lochhead, "Federal government to probe state spending on Delta tunnels," *San Francisco Chronicle*, April 11, 2016. Available at <http://www.sfgate.com/nation/article/Federal-government-to-probe-state-spending-on-7242043.php>. The Southern California Metropolitan Water District purchased some islands in the Delta region which were thought to be useful should the tunnels be constructed. There was litigation aimed at stopping the purchase, but it failed to block the purchase and the sale went through.

<sup>44</sup>"Governor Brown Delivers 2016 State of the State Address," January 21, 2016. Available at <https://www.gov.ca.gov/news.php?id=19280>.

### **Implementing New Programs**

Despite his words of frugality, California social spending has advanced under Brown, including especially a new state Earned Income Tax Credit (EITC). At the national level, the federal EITC – which dates back to the 1970s – amounts to an income subsidy for low-wage workers, giving them tax “refunds” that can be larger than the income tax that they pay.<sup>45</sup> A few states supplement the federal EITC with similar state-level programs. But California did not have an EITC until one was included in its 2015-16 budget, effective for the 2015 tax year, i.e., for tax returns due in April 2016.

### **Fixing the Past**

In addition, in 2013, Brown pushed through a system known as the Local Control Funding Formula (LCFF) by which state education support to schools is targeted at disadvantaged students (as opposed to an equal payment per student in all districts). Both programs – new money via EITC and the more exact targeting of existing money for school via LCFF – could be looked at as budgetary legacies of the governor in his final term. The 2016-17 budget proposal contained an element related to pre-kindergarten programs that also involved more targeting.<sup>46</sup> Beyond sending more targeted finance for schools, however, Brown remained a skeptic about reforms imposed from Sacramento by the legislature. *"If the parent screwed up things, and if the principal's no good, if the principal can't lead, if the superintendent isn't very good, if the local school board isn't so good, what makes you think that the Legislature can fix it,"* he said.<sup>47</sup>

### **Ballot Propositions**

In one case, prison sentencing, Brown seemed to be following a policy of correcting a legacy of his first iteration as governor, so-called “determinant sentencing” which he signed back in the day during his first term, and which contributed to the expansion and crowding of state prisons. The governor announced support for a ballot measure that would further the trend toward reduced sentencing aimed at the state’s

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<sup>45</sup>The EITC is a variant of the so-called “negative income tax,” but it applies only to the *working* poor. To be eligible, you must have employment income.

<sup>46</sup>The state mandates that school districts offer pre-K programs. The governor proposed that there would be block grants for early education. Districts wouldn’t be mandated to offer pre-K to all students. But families with incomes above a specified level could pay to enroll their children. Low-income students would not pay for enrollment. There was opposition to the pre-K plan in the legislature, but the governor continued to push it in the May Revise, as will be noted below.

<sup>47</sup>Judy Lin, “Jerry Brown on subsidiarity, meritocracy, and fads in education,” *CalMatters*, May 5, 2016. Available at <https://calmatters.org/articles/brown-what-makes-you-think-that-the-legislature-can-fix-it/>.

over-capacity prisons.<sup>48</sup> Projections from the Legislative Analyst indicated that the prison population under realignment was leveling off at around 130,000 into the near-term future. Before the realignment process, the inmate population had been about 166,000.<sup>49</sup> As for the inconsistency between what he did on sentencing in term 1 and in term 4 four decades later, Brown explained, *“Problems I create, I can clean up.”*<sup>50</sup>

But while the governor favored the new sentencing proposition, he opposed a school construction measure – also slated for the November 2016 ballot – which provided for issuance of \$9 billion of state bonds. It remained unclear, however, the degree to which Brown would actively campaign against the measure which was supported by construction firms and unions.

### **Medi-Cal Tax**

While there was contention over particular ballot measures, Brown was able to end the conflict over the special tax on health care providers that draws federal dollars to state Medi-Cal. Done properly, the tax ultimately reimburses the providers for the costs of the tax but brings about a federal match that net adds to state resources. The tax, which is a clear plus for California due to the federal subsidy (said to be over \$1 billion), needed a few GOP votes to provide the necessary two thirds margin. Ultimately, once agreement of all parties was obtained, the Medi-Cal tax was passed by the legislature and approved by federal authorities. However, part of the deal with hospitals was that an initiative would be placed on the November 2016 ballot requiring that the funding obtained through the tax had to be used for the intended purpose absent a two-thirds vote of the legislature.<sup>51</sup>

### **Fiscal Calmness Overwhelms Dysfunction**

What seems to matter most to public perceptions is a sense of calm in Sacramento – which mainly means budgetary calm. Specific achievements or controversies are known mainly to policy wonks and relevant interest groups. As noted, the state’s reconstruction of the Bay Bridge has been characterized by a series of scandals. Other recent scandals have occurred in the management of Cal Fire – the state’s fire prevention

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<sup>48</sup>The measure was opposed by some in the law enforcement community and challenged in court on various grounds. But it eventually made it to the November 2016 ballot.

<sup>49</sup>Legislative Analyst’s Office, “Overview of Population and Budget Trends for CDCR,” March 3, 2016. Available at <http://www.lao.ca.gov/handouts/crimjust/2016/Population-and-Budget-Trends-030316.pdf>.

<sup>50</sup>Christopher Cadelago, “Jerry Brown: ‘Problems I create, I can clean up,’” *Sacramento Bee*, April 11, 2016. Available at <http://www.sacbee.com/news/politics-government/capitol-alert/article71188862.html>.

<sup>51</sup>The initiative became Proposition 52.

and firefighting agency – and in regulatory oversight of public utilities. But public opinion about the governor and the legislature did not seem to reflect these governmental malfunctions.

An out-of-control leak of natural gas from an underground storage facility in southern California led to forced evacuation of homes in the Porter Ranch area. Moreover, the leak was said to produce a massive greenhouse gas emission – in the face of Governor Brown’s commitment to have California be doing the opposite. The leak raised issues of proper state regulatory supervision of utilities and whether there had been lax oversight in the Porter Ranch case. There was also controversy in the environmental community over the actions of Brown appointees to the Coastal Commission in removing an executive director regarded as an environmental champion.<sup>52</sup> But as in the cases of other state administrative issues, none of these environmental problems seemed to rub off on the governor. Brown’s public approval levels floated around 55% during the spring of 2016. In contrast, as Governor Schwarzenegger dealt with his final (crisis) budget in 2010, he had an approval rating of just 23%.<sup>53</sup>

Even the state legislature’s standing in public opinion – which is always below the governor’s – seemed unaffected by the conviction and removal of three senators, one of whom – Leland Yee of the Bay Area – entered federal prison in March 2016.<sup>54</sup> The only repercussion of the senate scandals was a ballot proposition (Prop 50) on the June 2016 primary ballot which permitted cutting off of pay to senators who were suspended for misconduct. The proposition was offered up to the public as a kind of *mea culpa* by the state senate and was passed in June by over three fourths of the voters.<sup>55</sup>

### **Minimum Increases**

On the other hand, the legislature acted in March 2016 to keep a minimum wage increase initiative off the ballot by negotiating with supporters of the increase and then passing a compromise that would raise the wage in steps reaching \$15/hour in 2023.<sup>56</sup> Minimum wage increases potentially raise state budgetary costs

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<sup>52</sup>It was reported that Brown felt annoyed at not being consulted when the executive director was originally hired several years earlier and so was happy to see him go. See Dan Weikel, “Here’s why the Coastal Commission director’s ouster didn’t upset Jerry Brown,” *Los Angeles Times*, April 14, 2016. Available at <http://www.latimes.com/local/california/la-me-coastal-commission-brown-20160414-story.html>.

<sup>53</sup>These ratings are for registered voters from the Field Poll: <http://www.field.com/fieldpollonline/subscribers/RIs2333.pdf> and <http://www.field.com/fieldpollonline/subscribers/RIs2543.pdf>.

<sup>54</sup>In the Public Policy Institute of California poll of July 2016, Brown had a 53% favorable rating among all adults and the legislature had 45%. See [http://ppic.org/content/pubs/survey/S\\_716MBS.pdf](http://ppic.org/content/pubs/survey/S_716MBS.pdf).

<sup>55</sup>When the three senators were indicted for various misdeeds, they continued to be paid under the law as it was then.

<sup>56</sup>There were actually two rival minimum wage increase initiatives sponsored by different labor union groups. Under the deal reached with the legislature, no minimum wage initiative would appear on the ballot. In the legislative deal, after the minimum wage reached \$15/hour in 2023, it would thereafter be indexed to inflation.

for a program by which the state pays for home care aides for the disabled. Such aides tend to be low-paid workers who would be affected by hikes in the wage floor.

### **External Events That Didn't Happen**

Two events might have affected trends in Sacramento in the lead-up to the May Revise, but didn't. A legal case had made its way to the U.S. Supreme Court that could have affected the resources available to public sector unions which are influential in state politics. Union members pay dues to their organizations. Workers who are not members, but are in bargaining units, nonetheless must pay "agency fees" that pay for the costs of representation, if the union contract so requires. Although this arrangement has long been supported by the courts, it was challenged and it appeared the Supreme Court would invalidate such fees. However, the death of Justice Antonin Scalia led to a 4-4 tie on the case and thus the fees were continued.

The other event was a report by the state auditor that opined that out-of-state students, whose tuition surcharge provides added revenue for the University of California (UC), were displacing in-state students. UC argues that out-of-staters are an addition to total enrollment and subsidize in-staters. The University adamantly disagreed.<sup>57</sup> The auditor's report could have had significant budgetary consequences for the University, whether its conclusions were valid or not. However, as it turned out, the controversy did not seem to have any effect on the May Revise which retained the governor's January budget proposal for UC.

### **New Estimates**

As noted early, at around the time of the January budget, revenues were running ahead of levels forecast when the 2015-16 budget was enacted. The governor upped estimates for the year as a result, perhaps hoping that the idea that there was extra money in the state treasury would not be the headline before the legislature. And indeed, as the May Revise date approached, revenues were a little *below* the January forecast levels. But they remained *above* the original forecast. By the time the May Revise rolled around, revenues were over \$2 billion ahead of the old forecast. In effect, legislators could choose whether they wanted to think of revenues as being above or below expectations. It depended on when they wanted to feel that their expectations were formed.

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<sup>57</sup>California State Auditor, "The University of California: It's Admissions and Financial Decisions Have Disadvantaged California Resident Students," March 2016, Report 2015-107. Available at <https://www.auditor.ca.gov/pdfs/reports/2015-107.pdf>. The report contains the UC response.

## The May Revise

*"It is best to prepare for the days of necessity."*

Governor Jerry Brown on the May Revise<sup>58</sup>

Not surprisingly, to the extent there was a choice concerning how to think about revenues, Governor Brown wanted the legislature to focus on the side of caution. No major new programs were included in the May Revise and the governor indicated that he wouldn't accept plans for such programs in the final version. Adding an extra \$2 billion to the rainy day fund beyond what the formula required was also part of the May Revise. On the other hand, noted earlier, the extra \$2 billion for the rainy day fund was essentially drawn from the regular reserve for the General Fund, so the shift from one to the other could be viewed as a matter of symbolism.<sup>59</sup>

Of course, it is impossible to know what the legislature might have proposed, or enacted, had the governor not signaled that his priority was fiscal prudence. Shortly before the legislature was due – under the constitution – to enact a budget, the state controller's report indicated that revenues for the first eleven months of the 2015-16 fiscal year were a bit below what the governor had forecast in the May Revise. But they were still \$1.7 billion ahead of the forecast in place when the 2015-16 budget was enacted.

And there was uncertainty concerning what voters might do in the November 2016 election. There might (or might not) be extra revenue compared to what was expected over the coming years *if* voters approved an extension of the income tax piece of Proposition 30 of 2012. The governor did not endorse the extension, nor did he oppose it. He just said he would manage either way, approval or not. However, the electorate would be voting on extending a tax that most of them did not pay: the top bracket of the personal income tax. So a legislator looking for a reason to be optimistic about future revenue might tilt toward an assumption of voter approval. And in terms of a ballot proposition that would save future money, signatures for the governor's initiative that would reduce penalties (and thus prison costs) were submitted to the secretary of state for verification shortly after the May Revise was made public.<sup>60</sup>

In the absence of a budget crisis, however, much of the state's political attention focused on the presidential races of both major parties until it became evident that the eventual candidates would be locked in by the

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<sup>58</sup>Office of the Governor, media release of May 13, 2016. Available at <https://www.gov.ca.gov/news.php?id=19417>.

<sup>59</sup>As previously noted, monies in the rainy day fund are harder to withdraw than those in the regular reserve. So an alternative interpretation was that the governor was trying to lock up the reserves.

<sup>60</sup>Opponents of the initiative attempted, but failed, to block it through litigation from appearing on the ballot.



time of the June California primary.<sup>61</sup> As noted, the one proposition on the June ballot dealing with suspensions of senators who had engaged in malfeasance was non-controversial and passed easily.<sup>62</sup> Gubernatorial energy was focused on such non-budget matters as a bill he proposed (but later failed to pass) that would have limited local review and approval of certain “affordable” housing developments. It became evident that there would be many initiatives on the November 2016 ballot and speculation mounted over which ones would in fact appear. Ultimately, there would be seventeen state propositions on the ballot.<sup>63</sup>

Cap-and-trade revenues from auctions fell notably below expectations. The governor’s high-speed rail and other programs depend on such revenues so the prospects for a revenue squeeze raised concerns. However, substantial revenues from prior auctions remained in reserve, so there was no immediate threat. But the cap-and-trade program under current law will expire in 2020 unless renewed, and Governor Brown was actively pushing for renewing legislation. Adding to the controversy was a report from UC-Berkeley that noted that cap-and-trade added to the costs of energy-intensive industries and thus tended to retard such economic activities.<sup>64</sup>

### **Final Passage**

*"This solid budget makes responsible investments in California and sets aside billions of dollars to prepare for the next recession"*

Governor Jerry Brown on signing the 2016-17 budget<sup>65</sup>

As expected, the legislature – operating in a non-crisis atmosphere – enacted a budget by the June 15 deadline. In fact, the budget involves more than one bill, and not all were passed on the deadline date. But a bill labeled the budget was passed, and that was all that was required constitutionally. Litigation a few years

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<sup>61</sup>Even when it became known who the two parties’ nominees would be, controversy continued. Some state Republicans were actively opposed to Trump even after it became apparent that he was their party’s nominee; others were noncommittal or supported him. On the Democratic side, some Sanders supporters complained about difficulties in voting procedures for independent voters. (Independents can vote in Democratic primaries.)

<sup>62</sup>Under current law, initiatives appear only on general election (November) ballots, but the legislature can put its own propositions on any ballot.

<sup>63</sup>The Service Employees International Union had circulated an initiative limiting executive compensation in the hospital industry as part of an effort to organize nonunion hospitals. However, the union had made a prior deal with the California Hospital Association (CHA) not to pursue such an effort. An arbitrator in June 2016 ruled that the union would have to cease promoting its initiative and withdraw it.

<sup>64</sup>Wayne Gray, Joshua Linn, and Richard Morgenstern, “Employment and Output Leakage under California’s Cap-and-Trade program,” Resources for the Future, May 2016. Available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2789820](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2789820).

<sup>65</sup>Office of the Governor, media release of June 27, 2016. Available at <https://www.gov.ca.gov/news.php?id=19463>.

earlier had established that it is the legislature that decides what a budget is.<sup>66</sup> Once the budget is passed by the legislature, even if all the pieces are not in place, the bill goes to the governor who can sign it, veto it entirely, or exercise his line item veto on components of the budget.<sup>67</sup>

Brown did not exercise any line-item vetoes, a decision which is highly unusual for a governor, even in cases – such as this one – in which there was an amicable accord in advance with legislative leaders.<sup>68</sup> Perhaps the details of budgeting were holding less fascination for the governor than they were earlier. He may have been focused on other Big Picture items. Shortly after the budget was signed, he opined on such matters as whether there should be compulsory public service for young people.<sup>69</sup> (He liked the idea.) And the *New York Review of Books* published a review by the governor on the dangers of nuclear warfare.<sup>70</sup>

### Continuing Evolution

Of course, passing the budget and signing it does not end the process. There remains implementation and the many detailed programs that make up broad categories such as “education.” As it does after a budget is put in place, the Legislative Analyst’s Office prepared a listing of hundreds of specific programs on which the legislature had provided directives.<sup>71</sup> These included such items as a report on options for diaper assistance for low-income families and another report on self-service terminals at the Department of Motor Vehicles. Various capital projects were authorized such as a new courthouse in El Centro and a lifeguard facility at El Capitan State Beach. Such items may seem to be minutiae, but ultimately budgets are the sums of such multitudes of individual programs and sources of revenue. And it matters how efficiently and effectively those programs are administered and revenues are raised.

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<sup>66</sup>Back in the crisis period of 2011, then-controller John Chiang had declared what the legislature had enacted as a “budget” by the deadline had technical irregularities and refused to pay the legislature for days without what he viewed as a flawed document. A subsequent court decision ruled that the legislature defines what a proper budget is, not the controller. But the missed pay was never returned to legislators.

<sup>67</sup>In 2011, Governor Brown vetoed the budget bill mentioned in the prior footnote. Both Brown and Chiang were heralded in the news media for rejecting a budget because it was not “balanced.” But Chiang’s rejection was based on technical issues, not balance. And the governor subsequently signed a budget containing the phantom \$4 billion in unknown revenue described earlier in this chapter.

<sup>68</sup>During his first iteration as governor, Brown had on one occasion refrained from any line-item vetoes once (in 1982, his final year.)

<sup>69</sup>David Siders, “Why Jerry Brown likes idea of mandatory service for young people,” Capitol Alert of *Sacramento Bee*, June 30, 2016. Available at <http://www.sacbee.com/news/politics-government/capitol-alert/article87008602.html>.

<sup>70</sup>Jerry Brown, “A Stark Nuclear Warning,” *New York Review of Books*, July 14, 2016. Available at <http://www.nybooks.com/articles/2016/07/14/a-stark-nuclear-warning/>. Although officially dated in mid-July, the review appeared on the web almost a month earlier.

<sup>71</sup>Legislative Analyst’s Office, “Supplemental Report of the 2016-17 Budget Act,” August 2016. Available at <http://www.lao.ca.gov/reports/2015/supplemental/2015-16-supplemental-report.pdf>.

The actual budget for 2016-17 will be different from what was put on paper in June 2016. Events keep occurring that affect the budget. Stock market returns, as it turned out, were anemic for the year ending June 30, 2016, causing increases in the unfunded liabilities of the major state pension plans. Certain undocumented persons who might have become eligible for Medi-Cal were blocked from doing so by a 4-4 U.S. Supreme court decision.<sup>72</sup> At this writing, it is unclear what the legislature may do regarding falling revenues from cap-and-trade and regarding extension of that program. And, of course, the path of the economy during the year will have major effects on the budget, primarily on the revenue side.

### **Voter Discretion**

Voters in November 2016 might or might not endorse the income tax extension of Prop 30 under Proposition 55. Other items on the ballot might also have budgetary significance, depending on what voters do. Marijuana might be legalized under Proposition 64 and potentially produce some tax revenue. Tobacco taxes might be raised under Proposition 56. The governor's proposed changes under Proposition 57 in criminal penalties might reduce prison costs. General obligation bonds might be approved for school construction under Proposition 51, imposing a long-term cost on the General Fund. When asked if voters would be confused by the large number of propositions on the November 2016 state ballot, Governor Brown responded, *"No more than usual."*<sup>73</sup> But there was uncertainty about what they would do, even if the uncertainty was "no more than usual."

### **Conclusions**

*"For all his efforts at creating a legacy, Jerry will probably be a chapter in the overall story of the Brown clan's impact on California. The main character in that story, however, will be his father, who was credited with building the best highway, water and state university systems in the nation."*

Former state assembly leader and former mayor of San Francisco Willie Brown<sup>74</sup>

Willie Brown – no relation to the "Brown clan" cited in the quote above – raises an interesting point. At the presidential level, we often associate names with achievements rather than infrastructure. Lincoln abolished

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<sup>72</sup>The Obama administration had created a deferred action program that gave temporary status to certain undocumented individuals. A lower court ruled the program illegal. The even split decision by the U.S. Supreme Court (one seat became vacant due to the death of Justice Antonin Scalia) meant that the lower court decision remained in place.

<sup>73</sup>David Siders and Jim Miller, "California voters face full plate of initiatives on Nov. 8," Capitol Alert of *Sacramento Bee*, June 30, 2016. Available at <http://www.sacbee.com/news/politics-government/capitol-alert/article87055132.html>.

<sup>74</sup>Willie Brown, "Why dump Chief Suhr? He's the best thing going for the SFPD," *San Francisco Chronicle*, May 13, 2016. Available at <http://www.sfchronicle.com/bayarea/williesworld/article/Why-dump-Chief-Suhr-He-s-the-best-thing-going-7468374.php>.

slavery and led the north to victory in the Civil War. The fact that the building of the Transcontinental Railroad was undertaken on Lincoln's watch is less noted or remembered. But, at the gubernatorial level, are *policies* – such as having a rainy day fund or targeting school monies toward the disadvantaged – what people remember in the long run? Or does legacy have to be tangible projects?

Willie Brown's quote doesn't deal with things people *don't* remember. They *don't* remember that Pat Brown left his successor (Ronald Reagan) with a budget crisis, even as they *do* remember Pat's highway-water-universities legacy five decades later. For that matter, Jerry Brown ran for the first term of his second iteration (in 2010) on the argument that his former political experience would allow him to resolve the budget crisis being left by Governor Schwarzenegger. The strategy worked because voters apparently forgot that in his first iteration, Jerry had left a budget crisis to his successor (George Deukmejian) to fix. While Jerry is obviously trying not to have another such crisis as the coda to his second iteration, if he succeeds in avoiding one – will that achievement be remembered? In fifty years?

For that matter, despite Jerry Brown's apocalyptic warnings about the dangers of global warming, will his efforts to reduce greenhouse gas emissions be remembered? Much of state policy on climate change is wrapped up in legislation and regulation, important components of which pre-date Brown's second iteration as governor. But there is no physical climate change monument for the coming generations to see. In contrast, Pat Brown's freeways, water project, and university campuses are still around and visible.

The history of Jerry Brown's father suggests that the high-speed rail and the water tunnels are more the stuff of public memory and legacy than is prudent fiscal policy. But the high-speed rail project, although it is currently under way, might never be completed. Much depends on future political leaders, both in Sacramento and Washington, D.C. There is no way for Jerry Brown to lock in that project before he leaves office in January 2019. The water tunnels are even less advanced than the train; as the 2016-17 fiscal year began, there was no final authorization for the tunnels let alone any actual construction.

Brown's first iteration focused on being tight with the dollar and skeptical about grand infrastructure projects. But being tight with the dollar ultimately couldn't prevent the combination of a state political crisis – Prop 13 of 1978 and the "taxpayer revolt" – and a national economic crisis – two back-to-back recessions in the early 1980s – from creating the budget disarray that he left behind. As Brown begins his planning for his next California budget – for fiscal year 2017-18 – he will have to weigh his past history – and his dad's.

Table 1: Enacting the 2016-17 Budget (\$Millions)

	LAO Outlook Nov. 2015	Governor Jan. 2016	Governor May 2016	Enacted June 2016
GF Starting Balance	+\$3,210	+\$5,172	+\$4,829	+\$4,874
Revenue & Transfers	+123,183	+120,633	+120,080	+120,310
Expenditures	-121,119	-122,609	-122,155	-122,468
Surplus/Deficit	+2,064	-1,979	-2,075	-2,158
GF Ending Balance	+5,274	+3,196	+2,754	+2,716
Rainy Day Fund				
Starting Balance	+5,641	+4,455	+3,421	+3,420
Ending Balance	+7,234	+8,011	+6,713	+6,714
Surplus/Deficit	+1,593	+3,556	+3,292	+3,294
Total				
Reserves				
Starting Balance	+8,851	+9,627	+8,250	+8,294
Ending Balance	+12,508	+11,207	+9,467	+9,430
Surplus/Deficit	+3,657	+1,580	+1,217	+2,716
Reserves/Expenditures	10.3%	9.1%	7.7%	7.7%

Source: <http://www.ebudget.ca.gov/2016-17/pdf/BudgetSummary/SummaryCharts.pdf>,  
<http://www.ebudget.ca.gov/2016-17/pdf/Revised/BudgetSummary/SummaryCharts.pdf>,  
<http://www.ebudget.ca.gov/2016-17/pdf/Enacted/BudgetSummary/SummaryCharts.pdf>,  
<http://www.lao.ca.gov/reports/2015/3305/fiscal-outlook-111815.pdf>.

Table 2: Accrual Data: General Fund and Rainy Day Fund Budgets (\$Billions)

	General Fund		Rainy Day Fund*		Total	
	Year End Balance	Surplus/Deficit	Year End Balance	Surplus/Deficit	Year End Balance	Surplus/Deficit
Brown Elected; Last Schwarzenegger Budget 2010-11	+\$3.1	+\$2.3	0	0	+\$3.1	+\$2.3
Phantom 4 Budget 2011-12	+\$1.6	+\$1.5	0	0	+\$1.6	+\$1.5
Prop 30 Taxes Passed 2012-13	+\$2.5	+\$4.1	0	0	+\$2.5	+\$4.1
2013-14 - Historical	+\$5.6	+\$3.1	0	0	+\$5.6	+\$3.1
2013-14 - Current**	+\$5.1	+\$2.6	0	0	+\$5.1	+\$2.6
Brown Re-elected 2014-15	+\$3.4	-\$1.7	+\$1.6	+\$1.6	+\$5.1	-\$0.1
2015-16	+\$4.9	+\$1.4	+\$3.4	+\$1.8	+\$8.3	+\$3.2
Projected 2016-17	+\$2.7	-\$2.2	+\$6.7	+\$3.3	+\$9.4	+\$1.1

\*Budget Stabilization Account (BSA)

\*\*Current data from [http://www.govbud.dof.ca.gov/2016-17/pdf/Enacted/BudgetSummary/BS\\_SCH1.pdf](http://www.govbud.dof.ca.gov/2016-17/pdf/Enacted/BudgetSummary/BS_SCH1.pdf); Historical data from [http://www.dof.ca.gov/budget/summary\\_schedules\\_charts/documents/CHART-A.pdf](http://www.dof.ca.gov/budget/summary_schedules_charts/documents/CHART-A.pdf). Historical data include unexplained "adjustments" of the balances reported on the official table.

Note: Data may not sum to totals due to rounding. A surplus is a positive change in the balance. A deficit is a negative change in the balance.

Table 3: General Fund Cash Budget and Rainy Day Fund Budget (\$Billions)

	General Fund		Rainy Day Fund*		Total	
	Year End Balance**	Surplus/ Deficit	Year End Balance	Surplus/ Deficit	Year End Balance	Surplus/ Deficit
Brown Elected; Last Schwarzenegger Budget 2010-11	-\$8.2	+\$1.8	0	0	-\$8.2	+\$1.8
Phantom 4 Budget 2011-12	-\$9.6	-\$1.4	0	0	-\$9.6	-\$1.4
Prop 30 Taxes Passed 2012-13	-\$2.4	+\$7.2	0	0	-\$2.4	+\$7.2
2013-14	+\$3.0	+\$5.4	0	0	+\$3.0	+\$5.4
Brown Re-elected 2014-15	+\$3.0	0	+\$1.6	+\$1.6	+\$4.6	+\$1.6
2015-16	-\$0.6	-\$3.6	+\$3.4	+\$1.8	+\$2.8	-\$1.8
Projected 2016-17	\$0.0	+\$3.6	+\$8.0***	+\$4.6	+\$8.0	+\$5.2

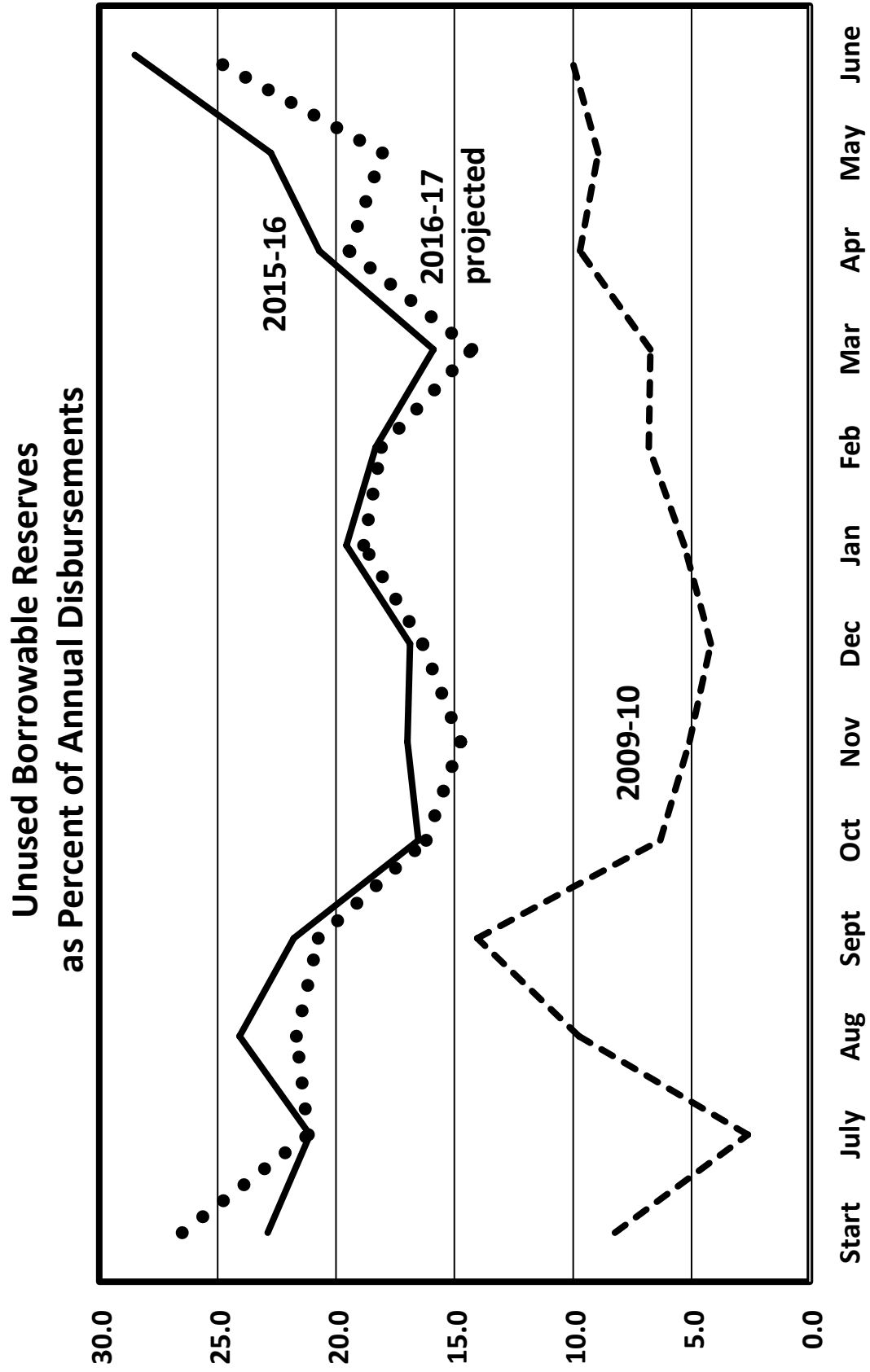
\*Budget Stabilization Account (BSA)

\*\*The General Fund is listed as having a zero balance when there are loans (external or internal) outstanding. The table above depicts outstanding loans as a negative balance. The "balance" refers to total cash in the General Fund.

\*\*\*Figure on cash basis. See source below.

Note: Data may not sum to totals due to rounding. A surplus is a positive change in the balance. A deficit is a negative change in the balance. Source of cash reports in the General Fund: [http://www.sco.ca.gov/ard\\_state\\_cash.html](http://www.sco.ca.gov/ard_state_cash.html). Rainy Day fund data projected for 2016-17 from [http://www.ebudget.ca.gov/2016-17/pdf/BudgetSummary/BS\\_SCH5D.pdf](http://www.ebudget.ca.gov/2016-17/pdf/BudgetSummary/BS_SCH5D.pdf).

Figure 1



Source: [http://www.sco.ca.gov/ard\\_state\\_cash.html](http://www.sco.ca.gov/ard_state_cash.html).





# CHAPTER 2

## Foundations in Los Angeles

**Helmut K. Anheier and David B. Howard\***

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*“Men and women have learned that there is no greater satisfaction than that of leaving a portion of their wealth to the lasting benefit of posterity.”*

The Los Angeles Community Trust, May 21, 1929

Modern foundations arrived in the Los Angeles region after they first developed on the East Coast and the Midwest where they had ushered in a new era of philanthropy. Benefiting from East Coast institutional innovations, but in an economy, society, and cultures being and becoming increasingly different, what patterns and roles did foundations in Los Angeles develop? The social, economic, and political concerns of the rising, growing metropolitan area of Los Angeles were and are unlike those of the Eastern United States, and also different from the California Bay Area or Washington State, which developed in rather distinct patterns. Did foundations emerge along lines similar to what has been observed for other parts of the country, or do we see a distinct profile?

This chapter first provides an overview of the history, scope, and role of foundations in the LA metropolitan area, and explores the extent to which the emergence of foundations in the region mirrors that of their counterparts outside the region. Post-World War II affluence spurred by federal investments in aerospace and defense, the emergence of Hollywood and other industries, and the attractiveness of LA’s climate and upscale communities help explain the growing presence of wealth in the region during the second half of the twentieth century. Today, LA’s philanthropic community is one of the largest in the country, with greater foundation numbers, assets, and grant dollars than most states.

We will then look at the present more closely, and find that despite the growth and absolute size of the local foundation sector, LA’s *per capita* foundation activity ranks in the middle of the country’s largest metro areas, and foundation giving has failed to outpace gross metropolitan product (GMP) growth going back more than a decade. We highlight the contributions foundations have made in the past and are making today. That analysis will generate a clearer understanding of roles they perform, and if, and how these roles might be different from other parts of the country.

## Los Angeles Background

Common descriptors of Los Angeles include dynamic, diverse, sprawled, decentralized, and unbalanced. A tremendous economic force and a leader in social and cultural trends, LA is a key international commercial hub, home to a strong industrial base, and the center of the U.S. entertainment industry. Los Angeles County—which includes the City of Los Angeles, 87 other cities, and numerous unincorporated areas—is by far the most populous county in the U.S., with about 10 million residents. LA County is also one of the most diverse counties in the country.

In addition to the expansive geography, large population, and vast economy, the nature of the local social sector and political fragmentation make the LA region an illustrative case for exploring the role of foundations and philanthropic efforts writ large. LA is one the most economically segregated regions in the country and so philanthropy could potentially play an important role in addressing critical issues related to the divide between poor and affluent neighborhoods. Income and wage disparity in the region conjures allegorical reference to the Dickensian dichotomy of the “haves” and “have-nots”—indeed a tale of two cities. (United Way of Greater LA, 2010).

The local nonprofit economy or sector, which represents about 6% of GMP (Gross Metropolitan Product), plays a critical role in providing an array of public goods and services, and many nonprofits—particularly larger agencies and institutions—rely on foundation grant-making (Anheier et al., 2013, Kil & Howard, 2010). The high demand for health and human services, education and schools, and arts and cultural offerings creates widespread opportunities for foundations. They can have an impact through supporting service delivery, advocacy and policy change, stakeholder convening, and promoting innovation.

This chapter will highlight several examples where foundation support continues to spearhead community-based initiatives, help build prominent institutions, fight for reform efforts, and provide critical financial support during times of economic downturn and government cutbacks.

We will also point out that LA foundations could have done more in the past, and that they are now in a process of searching for new modes to increase their contributions and impact.

### **Fragmented Government**

LA's governance fragmentation makes the emergence of public-private partnerships more difficult, and, indeed, such collaborations between public agencies and private nonprofit organizations generally, and between government and foundations in particular have been sparse (Osborn, 2010). Well into the early 21<sup>st</sup> century, and despite the growing importance of nonprofit organizations in higher education, health, and the arts, no overall pattern of nonprofit-government cooperation developed in a sustained and forward-looking way (Anheier et al., 2013). However, there are indications that this institutional weakness is being addressed and various initiatives suggest that changes are afoot in this respect.

In 2006, then-LA Mayor Antonio Villaraigosa appointed the first cabinet-level liaison to philanthropy. More recently, the Mayor's Office of Strategic Partnerships (OSP), funded by three local foundations, began working with a variety of entities to address issues related to transportation, housing, and job training—all with the intention of creating long-term change (Ferris & Williams, 2012; Osborn, 2010), and County-level initiatives followed. The OSP attracted private dollars (including support from the California Community Foundation) to expand programs like Summer Night Lights, a successful citywide anti-gang initiative.

### **Fiscal Problems**

Los Angeles also continues to feel the effects of Proposition 13, a 1978 state ballot initiative that restructured property tax laws, reduced local tax revenues, and made raising state and local taxes more difficult (Sweeting & Dinneen, 2013). The resultant atrophy of funding for state institutions and public services for low-income communities, funding that was further eroded by welfare reform legislation in the 1990s at the state and federal levels. Constraints on public funding led to pressure on foundations to fill the gap. In the wake of Proposition 13, funding for K-12 public education was particularly affected, as California fell well behind national averages in revenues and expenditures per pupil (California Budget Project, 2011; Wrigley, 2013). During

the Great Recession and its aftermath (2008-2011), the region's fiscal challenges were exacerbated by lower amounts of city revenue coming from property taxes (Sweeting & Dinneen, 2013).

### **Large Nonprofit Sector**

Amid a complex government structure, the LA region does have a large charitable sector—the largest nonprofit sector (in total numbers) outside of the New York metropolitan area, with nearly 32,000 nonprofits. It is a sector facing considerable challenges with respect to diversity, service capacity, and access (Hasenfeld et al., 2013). Indeed, as noted earlier, LA's nonprofit sector in per capita terms is lower than the national figures: only slightly below the number of nonprofits per 10,000 population, but 27% lower than the nonprofit expenditures per capita. Furthermore, many of LA's high-need areas also have the weakest nonprofit infrastructure—in terms of numbers and expenditures per capita (Anheier et al., 2008; Hasenfeld et al., 2013). This combination of high needs and low capacity challenges nonprofit funders.

Private foundations have been an important source of revenue for nonprofits in the arts and culture (Anheier et al., 2008). State funding of the arts has played a lesser role throughout, and stark cuts to the arts and arts education in the early 2000s created another gap that private foundations attempted to fill (Anheier et al., 2009). With per capita State spending on the arts in California among the lowest in the country, private foundations have nonetheless helped LA become home to many major arts and cultural institutions, including the J. Paul Getty Museum, the Music Center and Walt Disney Concert Hall in Downtown, and the Norton Simon Museum in Pasadena (Deener et al., 2013; Anheier et al., 2008). However, foundation support of the independent art scene of small nonprofit arts groups, including many small theaters and community arts centers, remains low.

In light of these distinctive traits, and as institutional philanthropy continues to evolve in the region, what trends have emerged and what role have foundations played in LA's social and

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Source: National Agency of State Arts Agencies, 2013. State Arts Agency Legislative Appropriations Preview Fiscal Year 2014. Available at <http://www.nasaa-arts.org/Research/Funding/State-Budget-Center/FY2014-Leg-Approp-Preview.pdf>.

political development? And how do these trends and roles compare to other regions in the country?

### **A Brief History of Foundations in Los Angeles**

Data from the Foundation Center's first edition of the *Foundation Directory*, which was published in 1960, show that New York City foundations represented nearly one quarter of all foundations at the time. They controlled 62% of total assets and over half (53%) of all grant dollars. In contrast, Los Angeles County had 3.1% of the nation's foundations, representing less than 1% of all assets and 1.5% of grants. The foundation community in Los Angeles in 1960 was still, however, one of the largest in the country. At the time, fewer than ten *states* had more foundations or more total grant dollars than Los Angeles.

Over the next 50 years, Los Angeles foundations increased their share of the nationwide philanthropic sector, albeit modestly. By 2011, LA foundations' national share grew in terms of numbers, assets, and total giving, to 4%, 7%, and 4%, respectively. The East Coast is still home to many of the most well-known foundations in the U.S. Names such as Broad, Keck, Ahmanson, and Weingart may not resonate with the national public the way Gates, Ford, Rockefeller, and Carnegie do. But a number of LA-based foundations have been and remain influential actors in areas including the development of institutions of higher education and arts and culture, and promoting reform efforts in health and education.

To be sure, the most-studied of the twentieth century foundations reside in the Northeast, although several prominent foundations are located on the West Coast. In 2011, four out of the top ten foundations in the U.S. (in terms of assets) were on the West Coast (of which three are

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Data contained in The Foundation Directory (Edition One) have some notable limitations and should be interpreted with some caution. The Directory excludes "very small" foundations, defined as those foundations that neither possessed assets of \$50,000 nor had made grants of at least \$10,000 in the latest year of record. Foundations in the Center records totaled approximately 12,000 in 1960, but The Foundation Directory, Edition 1, includes just 5,202 of these. Furthermore, some suggest that because data were at times difficult to collect, particularly in the Southern and Western regions, there may be a large portion of organizations unaccounted for in these data.



in California). But just one of the three—the J. Paul Getty Trust—is based in Los Angeles. Since LA’s largest foundations tend to invest grant dollars locally, and very few foundations engage in significant international grant-making, local funders have not developed nationwide recognition.

### **Two Periods of Formation**

Examining the trajectory of private foundation establishment in the region highlights two distinct periods in which the largest foundations—those with current assets in excess of \$100 million—were formed: the 1950s and the 1990s. As is the case nationally, the majority of foundations currently operating in LA—more than three-quarters (77%)—were established after 1990. The 1990s technology-driven economic boom allowed for an increased accumulation of wealth and accompanying incentives to form charitable foundations. Yet unlike in Silicon Valley and the Bay Area, the new growth industries (information technology) in Los Angeles were much less concentrated. It was also less characterized by an entrepreneurial renaissance to carry over from the world of start-up businesses to philanthropy. The region saw minimal formation of new types of philanthropic vehicles in the last two decades.

### **Early History**

In the early twentieth century, a number of foundations were created in the California Bay Area (e.g., the Lux Foundation (1908), the Avery-Fuller Children’s Center (1914), Oakland’s Latham Foundation (1918)), but Los Angeles establishments were scarcer prior to the 1920s (Sitton, 1999). One exception was the Los Angeles Community Foundation (formed in 1915 and later renamed the California Community Foundation), which was one of the nation’s earliest community foundations (Sitton, 1999). In a May 21, 1929 letter to readers published in the *Los Angeles Times*, the Foundation was described as a “public trust, patterned after the similar community trusts ... [that] provides a medium through which anyone may make large or small donations, endowments or bequests.” By the 1940s, the California Community Foundation was

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It should be pointed out that Getty is an operating foundation that primarily funnels grant dollars into the J. Paul Getty Museum (the Getty Center and Getty Villa)—two of the cities most celebrated arts and culture centers—as opposed to a wider pool of grantees.

one of the nation's most active—ranking fifth in giving and tenth in total assets out of 73 community foundations surveyed in the U.S., Canada, and Hawaii (Los Angeles Times, 1941).

Independent private foundations, although not in great numbers, did emerge in the first half of the twentieth century in Los Angeles. The John Randolph Haynes and Dora Haynes Foundation was created in 1926 and is the oldest independent general purpose foundation in Los Angeles—and one of the earliest in California (Sitton, 1999). After moving to LA from Philadelphia in 1887, the Haynes' made their wealth in real estate and banking. A physician by trade and major Progressive reform figure, Dr. Haynes became a prominent advocate for workers' protections, direct democracy, and social justice for Native Americans (Hoffman, 2001). Others, like George Pepperdine (see below), pursued more conservative objectives, and would leave their own indelible impacts on the region.

The Southern California oil industry created pockets of wealth that fueled significant philanthropic investments. G. Allan Hancock funneled his earnings from petroleum production into the Allan Hancock Foundation for Marine Research at USC (now the Hancock Institute for Marine Studies). He also donated a vast amount of land (including the La Brea Tar Pits) for public use (Hoffman, 2001). George Pepperdine, who made millions in auto part sales, established the George Pepperdine Foundation in 1931, and in 1937 the foundation funded the construction, endowment, and operating costs of Pepperdine College—now Pepperdine University (Lemley, 2010).

### **Religious Foundations**

The Pepperdine Foundation also represents a faction of substantial religious-based philanthropies that have created an impact in Los Angeles. A lifelong member of the Churches of Christ, Pepperdine founded his namesake university in part to “to place adequate emphasis and greater stress upon religious teaching and Christian character.”<sup>7</sup> Similarly, Conrad N. Hilton, the international hotel magnate and a devout Catholic, established his namesake trust in 1944 (later becoming a foundation in 1950) with a mandate to relieve the suffering, the distressed

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<sup>7</sup>Source <http://www.pepperdine.edu/about/our-story/history/>.

and destitute. Over the decades, the Hilton Foundation has remained committed to, among other causes, supporting the Catholic Sisters, a group that had profoundly influenced Hilton since childhood.

In 1949, Carrie Estelle Doheny, after she and her husband, oil tycoon Edward Doheny, commissioned and funded the construction of St. Vincent de Paul Church in Los Angeles, established her namesake foundation. The Doheny Foundation continues to be one of the region's largest supporters of religious causes. The Dan Murphy Foundation, incorporated in 1957, has been one of the largest supporters of the Roman Catholic Diocese and Archbishop over the years. In addition, Jewish philanthropy has produced prominent contributions to the region. The Jewish Community Foundation (mentioned later), was founded in 1954 and has become one of the region's largest foundations with assets of more than \$1 billion.

### **Entertainment**

The entertainment industry has also played a large philanthropic role in Los Angeles, even if Hollywood's foundation giving has been less than commensurate with the industry's revenue-generation. The Entertainment Industry Foundation (EIF), founded in 1942 by Samuel Goldwyn and other influential Hollywood figures as the Permanent Charities Committee of the Motion Picture Industry, illustrates an early philanthropic effort of the entertainment studios and industry to help maximize Hollywood's generosity during the Second World War (Aft & Aft, 2004; Ferris, 2010). In 2012, EIF contributed more than \$33 million in grant funding to a range of charitable causes. Hollywood's impact on private foundation grant-making is discussed later in the chapter.

### **Public Attention**

Following the rapid growth of the philanthropic sector in the 1950s, foundations became the target of widespread scrutiny from government and the public alike. Foundation leaders in Southern California established the Los Angeles Inter-Foundation Center (now known as Southern California Grantmakers) in response to the growing demand for regulation and

scrutiny of private foundations in the 1960s and 1970s. Note that nonprofit entities receive tax-favored treatment from all levels of government.

### **The Nineties**

Consistent with nationwide trends, LA foundations experienced tremendous growth—including a proliferation of foundation establishments—during the 1990s. The health of the economy and the dot-com boom help account for the philanthropic expansion in the region, but other trends played a part in the growth as well. Beginning in the late 1970s, a nationwide series of conversions of Blue Cross healthcare companies to for-profit corporations spawned a number of new private foundations over the next two decades. The two largest foundations to emerge from the conversions are located in the LA area and serve the state of California. In 1992, after Health Net’s nonprofit-to-for-profit conversion, the company was required to endow more than \$300 million into a foundation—the California Wellness Foundation. Since that time, California Wellness has awarded more than 5,700 grants totaling more than \$719 million in support of health promotion, wellness education, and disease prevention. In 2011, foundation assets were valued at nearly \$800 million.

When Blue Cross of California created WellPoint Health Networks, a for-profit corporation, the California Endowment was created. The Endowment’s assets represent 44% of the aggregated assets of the top 25 “new health” foundations in the U.S. In 2006, the Endowment opened a new facility in Downtown LA—the Center for Healthy Communities—which provides a state-of-the-art meeting space for nonprofit-related events and houses several prominent local nonprofit and philanthropic organizations (e.g., Southern California Grantmakers, the Center for Nonprofit Management, and Community Partners). The Endowment’s assets were valued at close to \$3.7 billion in 2011, making it by far the largest of the “new health” foundations in the nation and the largest independent private foundation (in terms of both assets and giving) in Los Angeles (Foundation Center, 2013).

## **Wealthy Philanthropists**

Although the two health conversation foundations in LA represent the bulk of the region's sectoral growth in the 1990s, several other prominent foundations emerged during the decade. Michael Eisner—former CEO of the Walt Disney Company—formed the Eisner Foundation in 1996 with his wife, Jane. Leonard I. Green, a pioneer in the development of the leveraged buyout industry, established the Green Foundation in 1994. Globally, Los Angeles is best known for being one of the world's entertainment capitals—with Hollywood at the epicenter of the entertainment industry.

The presence of Hollywood certainly has implications for local philanthropy, and even if the industry hasn't produced the largest local foundations, substantial grant-making foundations have become philanthropic vehicles for many successful artists, producers, and the like. Examples include The Wasserman Foundation (founded by Lew Wasserman, a prominent Hollywood agent with Music Corporation for America (MCA), and his wife, Edie; assets greater than \$180 million), The John W. Carson Foundation (created by former *Tonight Show* host Johnny Carson; assets greater than \$160 million), and The David Geffen Foundation (with assets greater than \$90 million).

The motion picture industry represents just one piece of a vibrant cultural scene and arts economy in Los Angeles. Private foundations, as philanthropic vehicles for wealthy LA residents, have provided key funding streams for many of the city's most beloved cultural centers: the Dorothy Chandler Pavilion, Mark S. Taper Forum, Ahmanson Theatre, Walt Disney Concert Hall, the Skirball Cultural Center, the Norton Simon Museum, the Broad Contemporary Art Museum, and others.

## **The Scale and Scope of Foundations in LA**

The history of independent grant-making foundations in Los Angeles dates back nearly a century, and the evolution of institutional philanthropic scope in the region has very much been a product of social and economic climate change. The emergence of the very large, well-known LA-based foundations largely followed national trends in the post-war 1950s and the growing

economy of the 1990s. This section charts the current scale and scope of foundations in Los Angeles, using data from the Foundation Center’s Statistical Information Service and Grants Sample Database.

## **LA as Number Two**

The Los Angeles metropolitan area’s foundation community makes a strong case for consideration as the country’s second largest behind the New York metropolitan area.<sup>1</sup> While New York ranks highest—by far—in terms of the number of foundations, total assets, and total giving, LA ranks fourth, second, and fifth in each respective category. Table 1 shows that LA, Chicago, and San Francisco run fairly close behind New York in most categories. Due to the Gates Foundation, Seattle ranks highly in both assets and giving.

The overall number of foundations—inclusive of independent private, operating, corporate, and community foundations—in the LA metropolitan area more than doubled between 1997 and 2011. Independent private foundations (126%) and community foundations (125%) more than doubled, while corporate foundations (71%) grew more modestly in terms of numbers. The number of operating foundations nearly tripled (169%). Overall, the number of LA foundations grew at a similar rate as the San Francisco metropolitan area (127%), and at a faster rate than the State (113%) and the U.S. (85%).

Figure 1 shows that in 2011 there were more than 3,100 foundations in the LA area. In terms of annual growth rates, the most considerable growth occurred between 1999 and 2001—the heart of the dot-com boom. During the Great Recession (2008–2011), growth rates remained stagnant before a slight uptick in 2011. While LA foundations are impressive in absolute terms, on a per capita basis, however, they appear less prominent nationally. In terms of the number of foundations per 10,000 population, assets per capita, and giving per capita, LA ranks 20<sup>th</sup>, 10<sup>th</sup>, and 14<sup>th</sup>, respectively.

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<sup>1</sup> Prior to 2004, the LA metropolitan area, as designated by the U.S. Office of Management and Budget (OMB), included both Los Angeles County and Kern County. In 2004, the LA metropolitan area was modified to include Orange County and no longer included Kern. The significance here is that Orange County has a much more robust philanthropic sector than Kern (a sparsely populated and highly mountainous region of the state). In 2004, Kern County had 64 private foundations that filed a 990-PF while Orange County had 714 filers.

Between 1997 and 2011, total foundation assets in the LA metropolitan area grew by 48%, adjusted for inflation (see Figure 2). Despite greater relative growth in the number of foundations, asset growth among LA foundations was higher than nationwide growth (37%) and on par with statewide growth (51%), but lower than growth among San Francisco Bay Area funders (82%).

Foundation assets experienced a precipitous decline when the dot-com bubble burst in 2000. Assets dropped 17% between 2000 and 2002, but experienced a steady increase between 2002 and 2007 (average annual growth was over 8% during that time). However, assets dropped again—by 9%—during the economic downturn in 2008 and 2009, and only rose slightly from 2009 to 2011.

Total giving by LA foundations more than doubled from 1997 to 2011, closely following asset growth patterns over time (Figure 2). During both economic downturns reflected in Figure 2, giving levels proved steadier than assets. In 2008, while assets dropped by 9%, giving actually rose by 11%, before experiencing a decline.

Despite overall growth of the sector since 1998, the value of foundation grants has struggled to keep pace with economic growth of the LA metropolitan area. As shown in Figure 3, growth in foundation grant dollars has fluctuated in terms of its share of Gross Metropolitan Product (GMP) in recent years. Between 2006 and 2008, foundation grant share of GMP rose by 32%, but 2009-2010 witnessed a steep drop in share of GMP. So while the importance of foundations relative to government overcame a steady decline in the years preceding the great recession, the share of GMP reverted back to 1998 levels by 2011.

Despite the economic downturn, notable local philanthropists such as Edythe and Eli Broad and Michael and Lori Milken have used foundations as vehicles to maintain and even quicken the rates at which they make large gifts to a variety of institutions. Both of these examples are couples that have signed onto the Warren Buffet- and Bill and Melinda Gates-inspired Giving Pledge.

## **Top Recipients**

As is the case in most areas of high philanthropic investment, the top recipients of foundation grants year-to-year tend to be universities (Table 3). From 2009-2011, the top four LA-grant recipients (and eight of the top 20) were universities. The University of Southern California (USC) received the largest amount of total grant dollars in 2011 (more than \$218 million)—the 4<sup>th</sup> highest total in the U.S. Also reflected on the list are several arts and culture institutions and two prominent private hospitals.

While LA boasts a large foundation sector in absolute terms, on a per capita basis— and based on growth relative to GMP, the sector is less impressive. Giving trends reflect patterns of asset growth in relation to economic conditions, although there is evidence that giving levels tend to sustain themselves even as assets experience declines. (This trend is consistent with national patterns as well. Overall, the results of the grants database reveals that LA foundations do not differ significantly from the national pattern. With some notable exceptions, such as health and human services, foundation grant-making is more or less comparable to that of the nation. In the next section, we examine more closely the role of foundations in LA, and provide some qualitative support and explanation of the quantitative analysis.

## **Foundations Roles**

One important way to assess how LA foundations differ from other regions of the country, in the aggregate, is to look at their roles or contributions. Anheier and Hammack (2010) and Hammack and Anheier (2013) proposed a classification of foundation roles, and this section explores how LA foundations fall into a variety of role categories. In general terms, this chapter examines illustrative examples of charitable relief efforts—foundation initiatives that largely complement or supplement government spending—and philanthropic efforts that spur innovation, pursue systemic change, and promote social justice and equality (Hammack & Anheier, 2013).



## **Immediate Relief**

One of the largest areas of foundation activity in LA—particularly in the human services domain—occurs through relief efforts focused on the immediate needs of various marginalized populations. Through these initiatives, some of which are described below, foundations tend to supplement government funding or services. Philanthropic contributions in dollar amount terms do not measure up to the government support of programs that address issues such as homelessness and health care. But foundation-funded efforts have spearheaded programs that have later attracted more public dollars.

For example, the Conrad N. Hilton Foundation has granted approximately \$42 million over a 20-year period to support local solutions to long-term homelessness. These grants have largely supported permanent supportive housing initiatives that have complemented funding efforts by local government. While certainly a generous contribution, the \$40-plus million multi-year commitment reflects just a fraction of the annual LA funding from the U.S. Department of Housing and Urban Development (about \$90 million) and the region’s estimated \$875 million in public spending on homelessness (United Way of Greater LA, 2012). But the support has also included cost-benefit research that has influenced greater public investment in solving the problem (e.g., LA County’s Project 50, which led to a \$105 million commitment from the County).

## **Building Out Institutions**

Particularly in the fields of higher education and the arts, LA foundations have provided substantial support for expanding local institutions. As indicated earlier, local universities are the largest recipients of foundation grant dollars. An analysis of the largest grants (\$1 million or more) made to LA-based recipients over the last decade shows that both the California Institute of Technology and USC have received close to \$500 million each from foundation grants of that size. The W.M. Keck Foundation alone has donated nearly \$300 million to USC.

As mentioned, foundations play an important role in the LA arts and culture sector—the second largest arts economy in the country (behind New York). Foundations in the LA region have also

stepped in to supplement reduced government spending on the arts, particularly in the area of arts education. Arts and culture organizations in LA are more dependent on foundation dollars than arts organizations nationally. While private foundation grants make up about 2% of the LA County nonprofit sector's overall revenue, foundation support accounts for 12% of the arts and culture nonprofit revenue (compared to 8% for the country as a whole) [Anheier et al., 2008].

When the California Arts Council budget was virtually eliminated in 2003, exacerbating previous cuts to public arts education funding, a number of private foundations offered significant support as a way to make up for lost public investment.<sup>1</sup> In 2005, while LA County arts nonprofits received less than \$250,000 in grant support from the California Arts Council, LA-based foundations gave more than \$40 million in local arts grants. Nearly 20 LA-based foundations alone exceeded California Arts Council funding to local organizations. In 2006, the Jewish Community Foundation and the Los Angeles County Arts Commission jointly funded over 150 arts residency programs in local public schools. The James Irvine Foundation—headquartered in San Francisco but with an affiliate office in Los Angeles—has also heavily invested in local arts initiatives.

LA foundations have made substantial investments in the region's cultural institutions, helping to build out LA's arts economy. From 2003 to 2013, local foundations have awarded the Los Angeles County Museum of Art, the largest art museum in the western U.S., more than \$150 million. In the late 1980s, Lillian Disney donated \$50 million toward what would become the Frank Gehry-designed Walt Disney Concert Hall—home of the Los Angeles Philharmonic and a critical ingredient in the redevelopment of Downtown LA (Deener et al., 2013). Between 2003 and 2011, the Walt and Lilly Disney Foundation granted nearly \$25 million to the Los Angeles Philharmonic.

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<sup>1</sup>Facing a major budget problem in 2003-04 in the wake of the dot-com bust, the California legislature enacted a number of deep cuts in spending. As a result, state General Fund support for the California Arts Council was reduced from \$18 million to \$1 million (a 94% reduction from the 2001-02 funding levels).

## **Policy Reform and Advocacy**

There are legal limitations on lobbying and political activities for nonprofit organizations. Nonetheless, private foundations have increasingly become involved with public policy in recent years. As a way to leverage philanthropic assets and in attempt to create longstanding “system change,” foundations have increasingly focused “on ambitions for transforming systems and producing substantial improvements in outcomes” (Ferris, 2003; Ferris & Williams, 2009).

Foundation watchdog groups such as the National Committee for Responsive Philanthropy have called on funders to direct more resources toward advocacy work and policy change. NCRP released a 2010 report on foundation support for advocacy, organizing, and civic engagement in LA (Ranghelli & Craig, 2010). Major foundations including the California Endowment and the California Community Foundation have embraced the idea of funding advocacy efforts. The Endowment requires such activity among all grantees.

## **School Reform**

In the wake of the federal No Child Left Behind law and as charter schools continue to emerge in Los Angeles, foundations have given more than \$250 million to school reform and charter school efforts in LA. The Broad Foundation has donated more than \$70 million to these efforts. In 2010, the Los Angeles Unified School District had more charter schools than any other district in the nation, with 183, serving 78,000 students (Wrigley, 2013).

## **Health Care**

Health care reform, particularly in relation to the roll-out of the Affordable Care Act, has also garnered substantial support and involvement from the local health-focused foundations in LA. The big health foundations—including the California Endowment (TCE) and the California Wellness Foundation (TCWF)—regularly support initiatives focused on pregnancy prevention, community violence reduction, promoting healthy aging, and other issues that address the needs of underserved populations and supplement government programs operated by the

County departments of Public Health and Mental Health. TCE and TCWF provide close to \$200 million annually to local nonprofits and coalitions working to improve access to quality health care, particularly among underserved populations, with a focus on public awareness campaigns, policy reform, and equitable healthcare. TCE has launched a partnership with The White House to ensure that the 15 million Latinos in California have sufficient access to and education about the new healthcare laws.

## **Social Justice**

Social justice change is another area where several LA-based funders have become increasingly involved. Whether in terms of ethnicity, income, national origin, or geography, high rates of diversity help define the LA region. Four funders—the California Community Foundation, the California Endowment, the California Wellness Foundation, and the Liberty Hill Foundation (a grant-making 501{c3} public charity)—have been particularly active in social justice funding. These funders have routinely offered support to local social justice organizations, including LAANE, Strategic Alliance for a Just Economy (SAJE), and ACORN (now the Alliance of Californians for Community Empowerment). The local health foundations have made recent investments in policy reform agendas that address local criminal recidivism and uninsured children (Raman, 2011). Issues related to advocacy and diversity are discussed further in the next section.

Increased calls for foundation transparency and accountability have crossed over into the realm of diversity—diversity with respect to foundation leadership, the organizations that foundations support, and the communities that benefit from foundation giving. Groups such as the Greenlining Institute and Diversity in Philanthropy have called for more support of minority-led nonprofits and for foundations to keep better track of diversity data (González-Rivera et al., 2008).<sup>1</sup> Greenlining, a public policy research and advocacy institute based in Berkeley,

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<sup>1</sup>According to the Greenlining Institute's (Aguilar et al., 2005) methodology, a minority-led organization is "one whose staff is 50 percent or more minority; whose board of directors is 50 percent or more minority; and whose mission statement and charitable programs aim to predominantly serve and empower minority communities or populations."

California, which receives funding from prominent foundations like Ford, California Wellness, and James Irvine, began releasing a series of reports in 2005 that analyzed numerous issues related to diversity and philanthropy. The initial report showed that of the top fifty independent foundations and the top 25 community foundations, only 3% awarded grant dollars to minority-led organizations (Aguilar et al., 2005). Interestingly, the report stated that corporate foundations, including the Wells Fargo Foundation, the Verizon Foundation, and the Washington Mutual Foundation, awarded more than 40% of their total grant dollars to minority-led organizations.

The reports issued by Greenlining led to a 2006 legislative hearing before the California Black, Latino, and Asian Pacific Islander Legislative Caucuses. Shared perspectives of foundation, nonprofit, and corporate leadership led in part to the introduction of Assembly Bill 624 by California State Assemblymember Joe Coto (a member of the California Latino Legislative Caucus) in 2007. The bill sought to monitor diversity-related philanthropic activities, prompting a number of local foundations to band together in opposition of the legislation. The legislation was eventually withdrawn when a coalition of nine foundations agreed to give at least \$30 million over three years to support minority-led nonprofits in addition to adopting a more strategic approach to building nonprofit leadership capacity among minority-led, community based groups (Wilhelm, 2008). The coalition includes some of LA's largest funders, including the California Endowment, California Wellness, the Ralph M. Parsons Foundation, the Annenberg Foundation, the Ahmanson Foundation, and the Weingart Foundation (Foundation Coalition, 2008).

The Funders Collaborative for Strong Latino Communities is another example of a philanthropic effort to reach a minority target population. Administered by Hispanics in Philanthropy, in 2004 the Collaborative awarded \$1 million to 13 Southern California-based Latino nonprofits, including the East Los Angeles Classic Theater in Monterey Park and Los Angeles-based Homies Unidos, to help build their organizational capacity and leadership.

## **A Place-based Approach**

Following the innovative models set forth by the Annie E. Casey Foundation and other prominent funders that have implemented place-based funding approaches, several LA-based foundations have begun to focus more on specific geographies. Perhaps one of the most poignant examples of a place-based strategy came about in the aftermath of the 1992 riots in Los Angeles—the worst local episode of civil unrest since the 1965 Watts riots. The Los Angeles Urban Funders (LAUF), a coalition of 18 foundations that included the philanthropies of three major banks, invested \$30-million into three low-income Los Angeles neighborhoods” — Pacoima, Vermont/Manchester, and Hyde Park (Anft, 2004). LAUF partners included the California Community Foundation, the California Endowment, the James Irvine Foundation, Liberty Hill Foundation, the Prudential Foundation, the Rockefeller Foundation, the Jewish Community Foundation, and Sony Pictures Entertainment. The LAUF model has been touted as an exemplar in collaborative funding, in particular due to its focus on community planning and resident involvement (Backer, 2001; Bernholz, 2004; Capek & Mead, 2007).

Place-based initiatives have become more commonplace over time. The California Endowment and California Community Foundation have adopted, to varying extents, place-based funding approaches. The Endowment has focused its grant-making on 14 communities throughout the state (three of which are in LA County). The Endowment’s Building Healthy Communities Initiative is investing \$1 billion over 10 years into 14 selected communities. The Foundation employed an extensive community selection process, which involved stakeholder engagement and community demographic and indicator research. The funding will benefit a range of challenged areas, including larger metropolitan areas like Sacramento and Long Beach in addition to smaller rural communities throughout the state.

In 2007, the California Community Foundation launched its Community Building Initiative (CBI) in El Monte, an underserved area of Eastern LA County. The Foundation engaged the community in an assessment and planning initiative, which helped craft a strategic plan to focus on youth and school support, health, and asset building. In addition to traditional grant-making,

CBI's goals include engagement with local government and leveraging further support from the private sector.

As place-based approaches have become more attractive to funders, other grant-making entities have followed suit. Notably, First 5 Los Angeles (F5LA), a public commission funded by tax dollars, focused on child-advocacy, has adopted a place-based approach for its most recent strategic plan. Though not a private foundation, F5LA has invested nearly \$700 million in the local community.

## **Conclusions**

Foundations in LA have played various roles over the past 60 years, helping to build out the region's largest cultural centers and universities, making substantial investments in health care access and policy reform, and strengthening the capacity of an over-burdened nonprofit sector, particularly in the human services area. They mainly serve in a complementary role to government, although coming close to a substitute for public investment in some cases, e.g., arts education. But foundations have helped promote and preserve higher education and arts and culture institutions, have sought strategic approaches by influencing public policy, have experimented with place-based approaches, and have provided key investments in building the nonprofit sector's capacity.

The LA foundation sector's development has shown both similarities and differences compared to broader national patterns. A pioneering era for philanthropy in Southern California occurred during a time of post-war affluence and industrial expansion. The economic boom of the 1990s, fueled in part by West Coast innovation, led to another surge in LA foundation activity and formation. Yet it was, and largely remains, a history of growing scale but not necessarily also growing importance, with two exceptions: first, health care and higher education, both fields with high concentrations on few recipient organizations, and second, a stronger emphasis on advocacy.

Of course, private foundations have had impact in a broad spectrum of institutions in Los Angeles. As the larger foundations in LA were not established until after World War II, many of

the region's major institutions, including some in higher education, were the products of philanthropy primarily. Yet the data presented here highlight the substantial foundation support of local universities as well as large cultural institutions—and increasingly so over time.

And while many of the region's largest foundations don the façades of significant cultural centers, schools, and social service facilities (e.g., The Broad Contemporary Art Museum, Disney Hall, the Weingart Center, the S. Mark Taper Amphitheatre, the Getty Museum, and USC's Keck School of Medicine and Annenberg School of Communications), such support has by and large remained rather conventional, and followed philanthropic trends from other regions. And while foundations have played important roles in response to crises such as the 1992 civil unrest in LA, with some exceptions they have yet to appear at the forefront of developments in philanthropy than other regions on the West Coast, especially the Bay Area.

Perhaps the question of what distinct and innovative pattern of grant-making seems to emerge in LA requires a shift in focus: above, we emphasized the track record of LA foundations in place-based philanthropy, and the experience of foundations working together, be it in response to the 1992 Riots or in the fields of arts education, mental health, or social justice. These initiatives seem to have set the course for what could in future become a pattern for philanthropy in LA, and perhaps become its hallmark: foundations that lead partnerships which involve government agencies as well as nonprofits—and even businesses—that are focused on particular fields or places.

Until the Great Recession, a somewhat curious conclusion we could have drawn about the role of philanthropy in the LA region was that it is much less daring, more conventional, less the innovator and more the adaptor, than the ever-changing, dynamic society of the region's millions of inhabitants represents. We would have asked whether LA foundations were in future able to deploy the creativity and innovative potential they undoubtedly harbored, and whether they were in the end able to make the contributions society rightly expected of them.

Nearly a decade later, LA foundations have made much headway. Despite the fragmentation of local government, persistent budget pressures, mounting social, economic and other problems



seemingly too big for private foundations to address alone, progress has been made. Such frustrating circumstances ultimately invited innovative responses among local foundation leaders, with the regional umbrella organization such as Southern California Grantmakers and university-led seminar series supporting their gestation.

These responses resulted in a still-emerging pattern that could perhaps be best described as the “coalition model” of philanthropy to leverage impact. It involves concerted efforts, spearheaded by foundations as well as others funders, and diverse coalitions of implementing agencies, be they public or private, for-profit or nonprofit. Whether LA foundation will be able to live up to the promise of the coalition model, and indeed, see it through its fuller development, remains an open question. But what the findings suggest is that the coalition model may well be the pattern that makes Southern California philanthropy distinct from New York and the Bay Area.

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**Table 1. Top 10 U.S. Metropolitan Areas, by Total Number of Foundations, Total Foundation Assets, and Total Foundation Giving, 2011**

Total Number of Foundations		Total Foundation Assets		Total Foundation Giving	
1. New York	9,775	1. New York	110,281,729,114	1. New York	10,302,577,629
2. Chicago	3,541	2. Los Angeles	44,294,554,972	2. Seattle	3,673,284,558
3. Philadelphia	3,460	3. Seattle	43,193,199,363	3. San Francisco	2,549,044,171
4. Los Angeles	3,112	4. San Francisco	29,532,585,488	4. Chicago	2,383,152,894
5. Boston	2,511	5. Chicago	26,828,549,246	5. Los Angeles	2,167,199,523
6. Pittsburgh	1,895	6. Philadelphia	21,700,960,358	6. Boston	1,260,986,550
7. San Francisco	1,842	7. Boston	17,196,308,760	7. Philadelphia	1,139,158,736
8. Miami	1,727	8. Minneapolis	14,224,700,783	8. Minneapolis	979,461,819
9. Dallas	1,706	9. Washington, D.C.	13,396,638,733	9. Houston	971,510,034
10. Washington, D.C.	1,610	10. Dallas	12,655,839,818	10. Washington, D.C.	927,309,679

**Source: The Foundation Center, 2013. The search set includes all active private and community grant-making foundations located in the state. Only grant-making operating foundations are included. Metropolitan Areas are designated by the U.S. Office of Management and Budget (OMB). Total giving includes grants, scholarships, and employee matching gifts.**

**Table 2. Number of Community Foundations, Total Community Foundation Assets, and Total Community Foundation Giving, U.S. Metropolitan Areas: Foundations with Assets of \$1 Billion or More, 2011**

	Metro Area	Number	Assets	Giving	Assets Per Capita	Giving Per Capita
1	San Francisco	4	\$2,806,081,323	\$209,133,739	\$639	\$48
2	New York	5	\$2,189,340,537	\$166,705,528	\$188	\$14
3	Cleveland	4	\$1,897,216,028	\$82,640,075	\$917	\$40
4	Chicago	14	\$1,860,706,299	\$117,775,177	\$196	\$12
5	Minneapolis	9	\$1,492,338,050	\$115,379,381	\$455	\$35
6	Los Angeles	9	\$1,366,337,020	\$158,385,855	\$106	\$12
7	Portland, OR	2	\$1,242,896,303	\$67,698,508	\$562	\$31
8	Kansas City, MO	2	\$1,190,121,242	\$220,815,373	\$589	\$109
9	Dallas	3	\$1,080,632,405	\$97,908,802	\$166	\$15
	Total		\$14,045,036,802	\$1,138,533,636	\$45	\$4
	% U.S.		24%	26%		

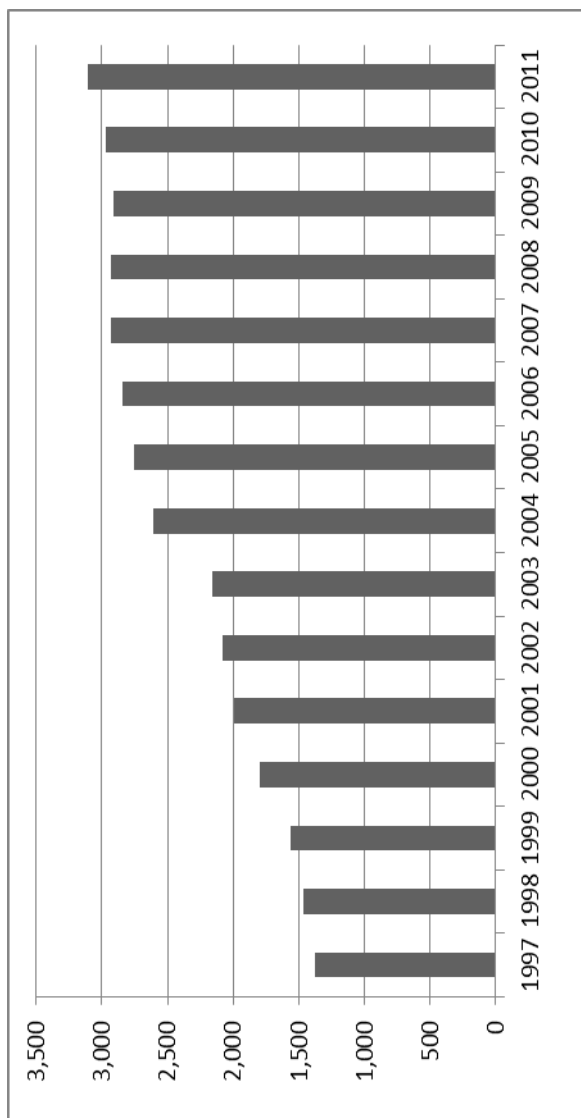
**Source:** Foundation Center, 2013. FC Stats: The Foundation Center's Statistical Information Service ([foundationcenter.org/findfunders/statistics/](http://foundationcenter.org/findfunders/statistics/)); U.S. Census Bureau, 2011: American Community Survey

**Table 3. Top 20 LA-based Foundation Grant Recipients, 2009-2011**

<b>Recipient Organization</b>	<b>City</b>	<b>Total Dollars Awarded (\$)</b>	<b>Number of Grants</b>
University of Southern California	Los Angeles	374,252,356	438
California Institute of Technology	Pasadena	173,734,421	203
University of California, Los Angeles	Los Angeles	143,146,237	371
UCLA Foundation	Los Angeles	83,727,642	196
Los Angeles County Museum of Art	Los Angeles	61,780,592	85
College-Ready Promise	Los Angeles	60,135,000	3
California State Polytechnic University	Pomona	42,000,000	1
University of California-Irvine	Irvine	38,021,760	86
Children's Hospital Los Angeles	Los Angeles	35,438,698	93
Skirball Cultural Center	Los Angeles	35,087,022	49
Claremont McKenna College	Claremont	34,737,256	73
Foundation for Global Sports Development	Los Angeles	30,000,000	1
California Charter Schools Association	Los Angeles	24,785,971	41
City of Hope	Duarte	23,968,957	30
Colburn School of the Performing Arts	Los Angeles	22,871,000	17
Green Dot Education Project	Los Angeles	16,707,384	20
Broad Center for the Management of School Systems	Los Angeles	16,412,517	4
Cedars-Sinai Medical Center	Los Angeles	15,906,433	37
Museum of Contemporary Art	Los Angeles	15,222,030	26
KCET Community Television of Southern California	Los Angeles	14,738,604	41

Source: The Foundation Center, 2009-2011. Based on all grants of \$10,000 or more awarded by a national sample of 1,339 larger U.S. foundations (including 800 of the 1,000 largest ranked by total giving). For community foundations, only discretionary grants are included. Grants to individuals are not included in the file. The data set searched includes only larger U.S. foundations.

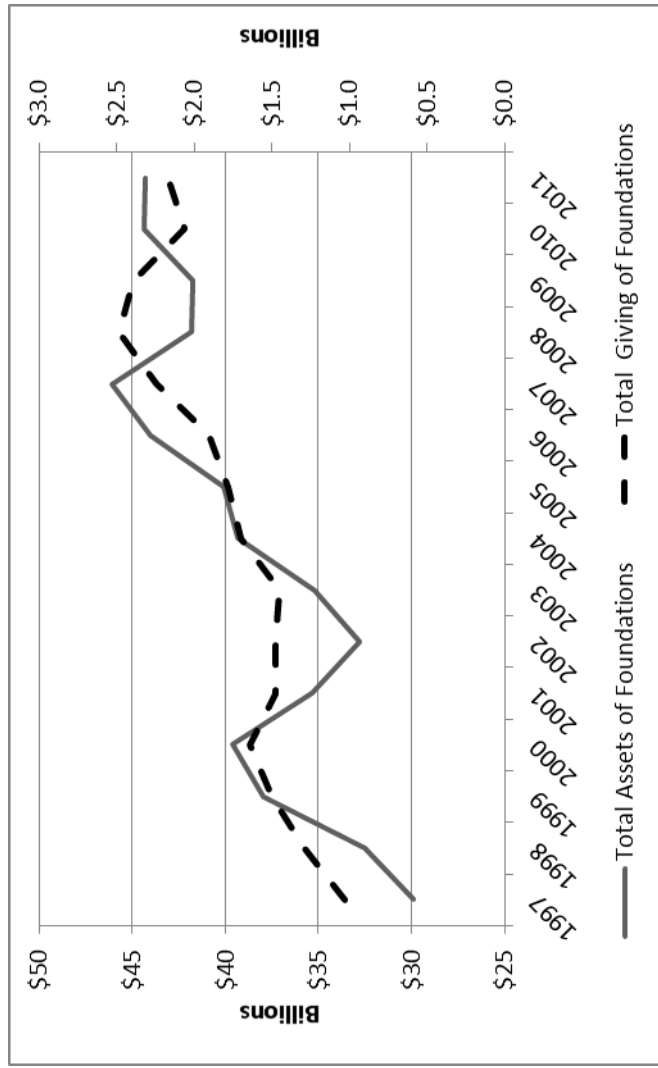
**Figure 1. Total Number of Foundations, Los Angeles Metropolitan Area, 1997-2011**



Source: The Foundation Center, 1999-2013

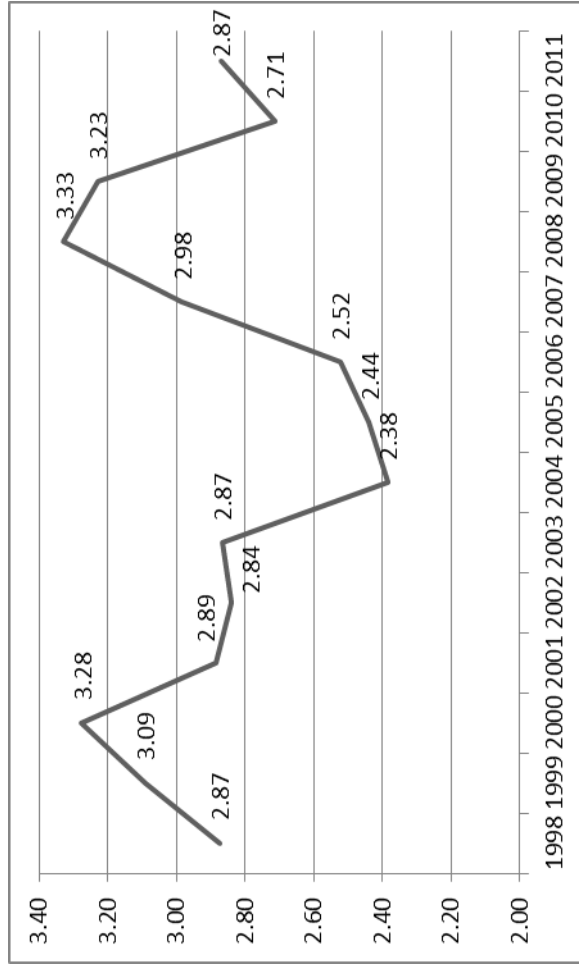


Figure 2. Total Foundation Assets (Left) and Giving (Right), Los Angeles Metropolitan Area, 1997-2011



Source: Foundation Center, 1999-2013. FC Stats: The Foundation Center's Statistical Information Service ([foundationcenter.org/findfunders/statistics/](http://foundationcenter.org/findfunders/statistics/))

**Figure 3. LA Foundation Grants per \$1,000 Gross Metropolitan Product (GMP), 1998–2011**



Source: The Foundation Center: FCStats, U.S. Conference of Mayors

Note: GMP data are shown for the Los Angeles-Long Beach Metropolitan Area for years 1998–2003 and Los Angeles-Long Beach-Santa Ana Metropolitan Area for years 2004–2007. (This coincides with Foundation Center’s GMP definitions). Analysis excludes: Grants less than \$10,000; grants made directly to individuals, expenditures for foundation-administered projects; community foundation grants from restricted or donor-designated funds; and grants awarded by private or community foundation to another U.S. foundation.



# **CHAPTER 3**

## **Better Than You Think: The California Outlook for 2017**

**Robert Kleinhenz and Christopher Thornberg**

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There is an obvious disadvantage in making an economic forecast before a major event such as a presidential election.<sup>1</sup> Depending on the outcome, national economic policy might shift – or might not. There is nothing at this writing in standard macroeconomic indicators that would suggest an imminent downturn in the national economy. But there are uncertainties stemming from national politics as well as developments in the Middle East and elsewhere that could affect the U.S. outlook and ripple down to California.

More locally, one measure on the November 2016 state ballot – if passed – could add to state revenue in the short term. But it would also continue the vulnerability of the state budget to the ups and downs of the real economy and financial markets since the added revenue would come from top earners.

Apart from events in the short term, there has been concern that the relatively slow growth after the Great Recession is indicative of a “new normal” in national economic performance. Is the earlier, faster pace of long-term growth now a thing of the past? If so, will California’s long-term growth rate, which until the end of the Cold War was notably faster than the national rate, ultimately be caught within that new normal?

Still, while there has been much talk about failings of both the national and state economies – talk that is stimulated in part by the election – current performance and the short-term outlook is better than you might think, given the critiques. There are indeed longer term structural issues that need addressing. At the state level there are issues of housing and infrastructure. And there are big national concerns such as accommodating and funding the retirement of the baby boomers. But whether or how those matters are addressed is more a matter of political forecasting than economic.

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<sup>1</sup> This chapter reflects information available as of early October 2016.

## **Solid Performance**

California stayed on course with a solid economic performance during the first three quarters of 2016, despite slower growth nationally. The state outdistanced the nation in terms of economic expansion and job creation. However, the pace of growth in 2016 in both California and the nation has been somewhat slower than in 2015.

Virtually every industry in the state continues to add jobs in 2016. The unemployment rate was lower than in the prior year and has been heading down towards levels not seen since before the Great Recession. All in all, the statewide economy is poised for continued growth into 2017, likely outpacing most other states around the country.

## **Overall Job Market Gains**

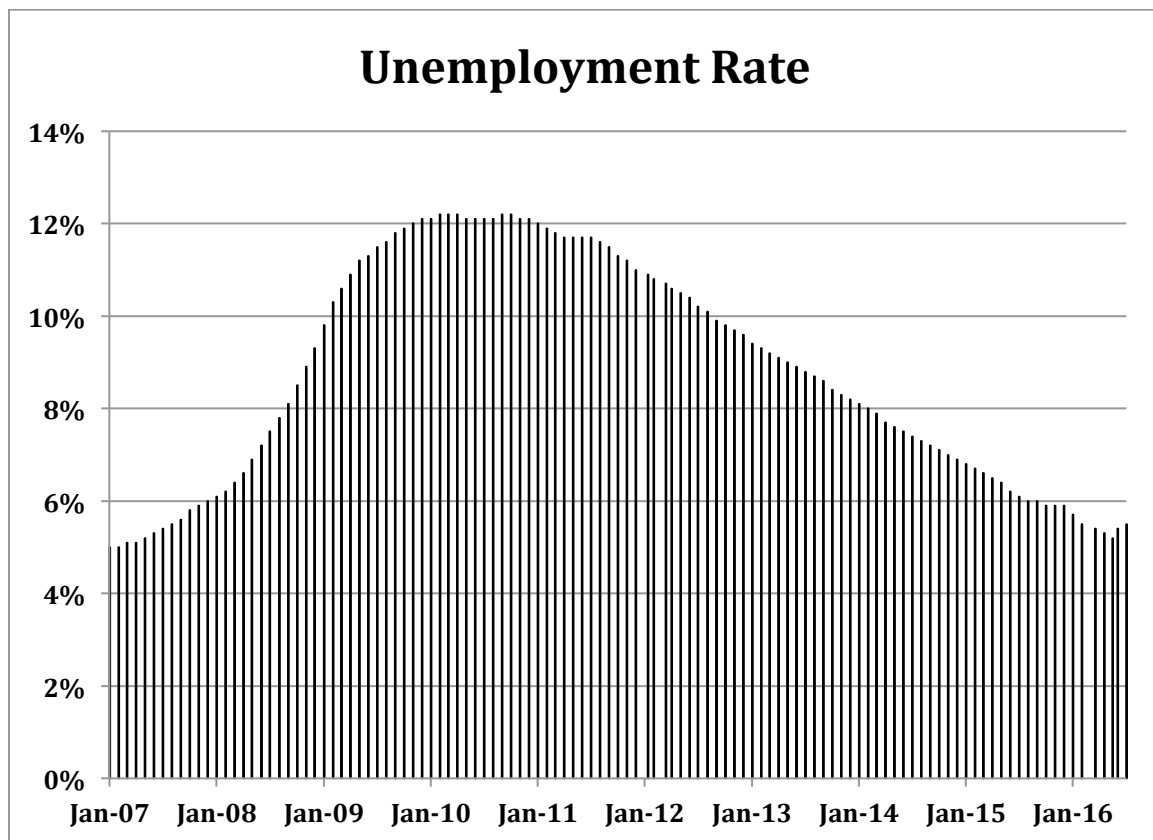
California's recovering job market has been particularly impressive during 2012-2016. Wage and salary (nonfarm) job growth exceeded the nation's each year in that period despite complaints about the state's business climate. In 2015, the state's 3.0% growth rate placed it among the top 10 states in the nation.

Through the first seven months of 2016, nonfarm jobs grew at 2.7% in California, compared to 1.8% nationally. As Figure 1 shows, the state's unemployment rate dropped below 6% late in 2015, moving into the mid-5% range for most of the summer of 2016. Moreover, sustained job growth and wage gains have drawn more people into the California labor force. It's not just the unemployed who have been obtaining new jobs.



*Hire UCLA: Job fair for students on October 5, 2016*

**FIGURE 1: Unemployment Rate Lowest in Years**





## Sectoral Job Expansion

The leisure and hospitality and health care and education industries led the way in 2015-2016 with the largest absolute job gains in the state, as can be seen on Table 1. Those advances were accompanied by significant contributions to the job pool from professional, scientific, and technical services, construction, and retail trade. In all, just two industry sectors lost jobs. Manufacturing and mining (essentially oil extraction) had combined losses of about 10,000 on a state nonfarm job base of 16.5 million, illustrating the breadth of job gains throughout the private economy. (Low oil prices account for diminished oil extraction activity.) Government was also among those sectors showing the largest absolute gains, with most of the increase occurring in state and local government. Many of the same industries led the state in terms of percentage gains, as well.

**TABLE 1: Industry Job Gains Continue, July 2015-July 2016 (000s)**

	July 2015	July 2016	Employment Change	Percent Change
<b>Total Nonagricultural Employment</b>	16114.4	16471.2	356.8	2.2
<b>Mining and logging</b>	28.7	25.2	-3.5	-12.2
<b>Construction</b>	732.1	763.3	31.2	4.3
<b>Manufacturing</b>	1298.1	1291.5	-6.6	-0.5
<b>Trade, transportation and utilities</b>	2948.3	2994.8	46.5	1.6
<b>Information</b>	484.8	495.0	10.2	2.1
<b>Financial activities</b>	800.9	812.9	12.0	1.5
<b>Professional and business services</b>	2506.0	2584.4	78.4	3.1
<b>Educational and health services</b>	2475.6	2558.5	82.9	3.3
<b>Leisure and hospitality</b>	1830.4	1896	65.6	3.6
<b>Other services</b>	547.0	551.8	4.8	0.9
<b>Government</b>	2462.5	2497.8	35.3	1.4

Source: Employment Development Department, news releases for August and September 2016

Perhaps surprisingly, California's agriculture sector has fared well despite the state's prolonged drought. Farm employment seems on track to hit its highest level in over a dozen years, and even farm earnings have held up well in recent years. Despite reduced water supplies, farmers have found ways to adapt.

### **Consumption**

In addition to steady job gains, spending activity statewide, as measured by taxable sales, has been growing steadily over the last few years. Taxable sales are a proxy for consumption although some forms of consumption are not subject to tax. Following an increase of over 4% last year, taxable sales were up by over 2% through the first half of 2016, with the busy holiday season still ahead.

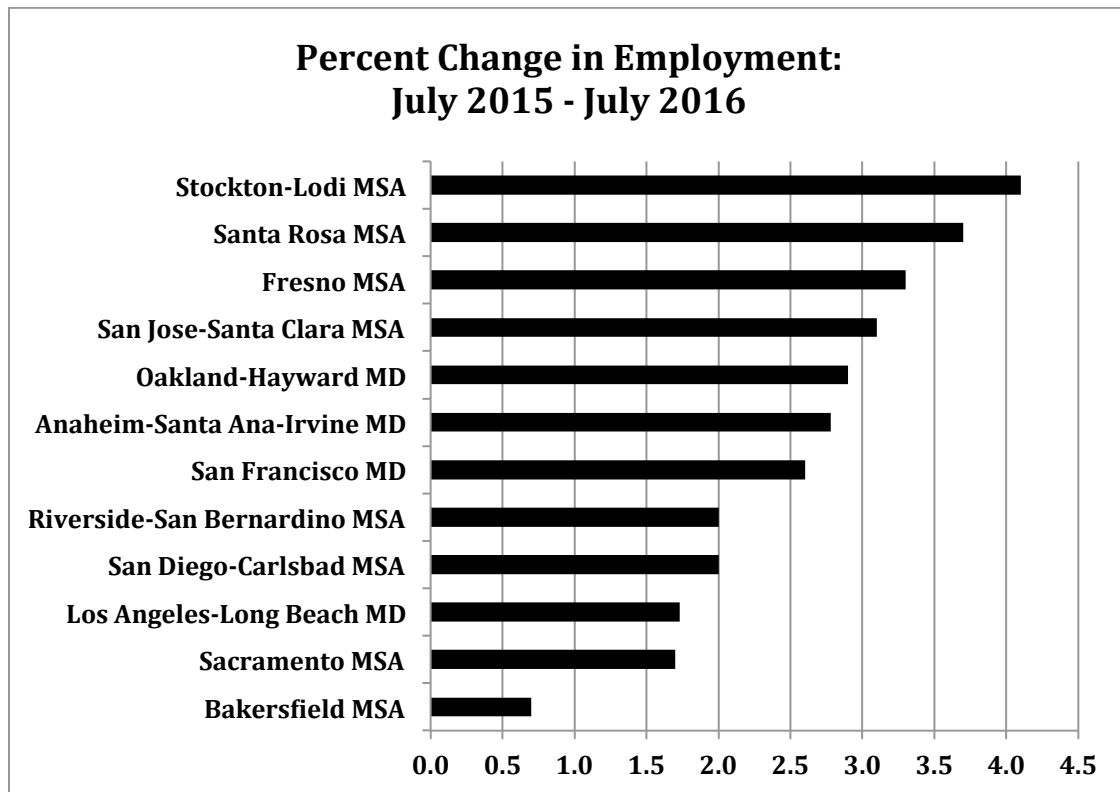
Not unlike the nation, the consumer sector accounts for most of the spending activity in the state. Taxable receipts on consumer goods accounted for 60% of total taxable receipts last year, and saw a modest 1.0% gain in the first quarter of this year. Taxable receipts by businesses registered a 5.4% increase over the same period, providing further evidence of the strength of the state's key industries.

### **Firing On All Cylinders**

Regional economies across California have grown over the last several quarters, with job gains that have varied across the state as shown on Figure 2. Some inland areas had been especially hard hit by the Great Recession. But economic growth has spread inland from coastal counties during 2015-2016. Many parts of the state have hit new records for employment and unemployment rates have declined to their lowest in several years. Smaller regions may lead the state in terms of percentage job gains. Los Angeles County routinely adds by far the largest absolute number of jobs from one month to the next because of its size. LA is followed by the Inland Empire, Orange County, and San Diego

County in the south and Silicon Valley (San Jose-Santa Clara) and San Francisco in the north.

**FIGURE 2: Job Gains Across the State by Area**



Note: MSA = Metropolitan Statistical Area. MD = Metropolitan Division

### **Room for Improvement in Housing**

The housing sector is important in its own right as a driver of California's economy. But it also serves as a gauge of the state's economic health. The picture for housing has been mixed since the Great Recession, which caused a major drop in home prices and a wave of foreclosure activity.

Home prices, shown on Figure 3, have advanced modestly in the post-Great Recession era despite many hurdles that have limited sales activity. Outside the San Francisco Bay Area, home prices have yet to surpass their pre-recession peaks. Demand for homes has

been sustained by continued low interest rates. But at the same time demand has been impeded by high underwriting standards for mortgages, and large down payment requirements. On the supply side, current homeowners in some areas have seen little reason to move and list their homes for sale, resulting in existing home supply that is well below long-run norms.

**FIGURE 3: Home Prices Up Modestly**

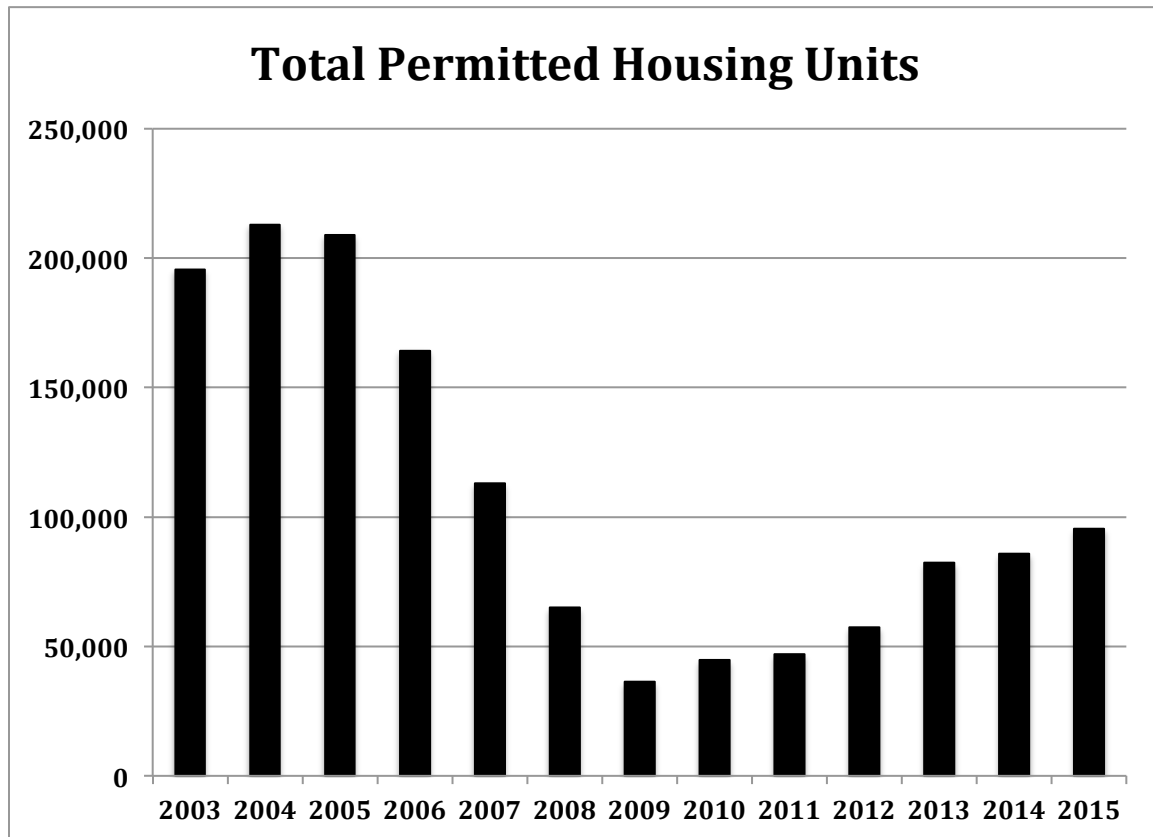
State/Region	Median Price			Sales*
	July 2015	July 2016	Percent Change	Percent Change
<b>California Existing Single Family Homes</b>	\$490,780	\$509,830	3.9%	-5.1%
<b>Los Angeles Metropolitan Area</b>	\$452,200	\$468,450	3.6%	-10.6%
<b>Inland Empire</b>	\$294,790	\$320,440	8.7%	-5.9%
<b>San Francisco Bay Area</b>	\$774,220	\$810,510	4.7%	-16.1%

\*Number of units sold.

Meanwhile, new home construction has struggled to advance since the recession as show on Figure 4, with building permit levels that remain well below the long-run average, mainly because of a very slow rebound in single-family home construction. Through the first half of 2016, total housing permits were 2.0% behind 2015, with a 10.6% decline in multi-family activity nearly offset by a much welcome 9.0% increase in single-family activity.

If there is any part of the residential market that is bursting at the seams, it is the market for rentals. Throughout many metro areas of the state, high demand for apartments has driven vacancy rates down and rents up. Rents continue to head north despite a significant increase in multi-family construction during 2014-2016. Despite the incentive to build stemming from rising rents, new supply has barely put a dent in the state's chronic and long-standing shortage of units. Although new construction is occurring, concerns about traffic and congestion have raised zoning and other political obstacles to a more rapid expansion of multi-unit housing.

**FIGURE 4: New Home Construction Recovering Slowly**



Demand for rentals has been strong in part because the market for owner-occupied homes has faced impediments as mentioned above. The homeownership rate was 54% in the first quarter of 2016, the lowest in over thirty years. This figure seems counterintuitive, given that the monthly payment for a typical home is well below its peak, owing to below-peak prices and historically low mortgage interest rates. But the tightening of lending standards – imposed after the excesses that led to the Great Recession – plays a role in holding down home ownership.

On the nonresidential (commercial) side of real estate, market conditions reflect the improvement seen across industry sectors and regions of the statewide economy. For both office and retail, vacancy rates have edged down quarter by quarter in the metro areas of the state, while lease rates have risen. Office lease rates in the San Francisco

Bay Area, Los County, and Orange County have led the way in terms of increases. At the same time, industrial vacancy rates in Los Angeles County are among the lowest in the nation, having declined steadily into 2016, while lease rates have been climbing by low single-digit yearly percentages.

## **Outlook**

In the short term, there is nothing in the data available at this writing that suggests a reversal of the ongoing expansion in California. The state's economic engine will likely chug along in 2017. Businesses and households have exercised greater caution in the post-Great Recession period compared to previous cycles. Perhaps that is not surprising since California was especially hard hit by that downturn. The state was disproportionately the home of the housing bubble and mortgage/foreclosure crisis. But since then, California's economy has consistently outperformed all but a few states around the nation.

The Tech sector continues to impress, not just in the Silicon Valley/Bay Area, but also in other parts of the state. Economic growth nationally will continue to drive the California's tourism and goods movement industries, while retail activity will see further gains as households across the state benefit from job growth and wage gains. Health care was largely insulated from the Great Recession. Demographics – the aging of the population – tends to support that sector. However, political uncertainties surround the expansion of health insurance under "Obamacare." California was especially aggressive in advancing coverage for the previously uninsured and thus demand for medical services.

The state continues to face nagging longer-run policy problems, not the least of which is housing. Rising home prices and rents signal that the state is not producing enough housing. The housing dilemma is not just a low-income problem, but one that extends to middle-income households as well. In many parts of the state, rent as a share of renter income exceeds the 30% threshold that is considered to be the norm.

In the market for owner-occupied homes, a household must earn at least \$100,000 annually in order to afford the payment on a median priced home in California. This issue has ramifications for employers who increasingly find it difficult to hire and retain qualified employees. The problem is particularly acute for employers that compete in national labor markets for talent. Solutions will be hard to come by, but must include reducing permitting and regulatory burdens associated with construction costs, and, possibly, tax reform.

In any event, the state tax system in its current form is highly dependent on the economic circumstances of a relatively small group of top income earners. It is thus subject to extreme sensitivity to the business cycle and perturbations in financial markets. The state has yet to address its large infrastructure needs such as transportation and water that must accompany housing needs. Addressing needs in transportation and water involves creating an appropriate funding mechanism. Tax issues and infrastructure issues are tightly bound up together.

As noted at the outset, political uncertainty surrounding the 2016 election extends into the economic sphere. For California, especially southern California with its large logistics industry connected to its seaports and airports, disruptions in international trade patterns could have an adverse local effect. The 2016 election has focused attention on the long-term shrinkage of manufacturing job opportunities. In absolute terms – not percentage – California has the largest manufacturing sector of any state. So the debate on that issue is not just a concern for Midwestern “rustbelt” states.

In short, there are many immediate bright spots in the economic outlook for California. But it is not exempt from the concerns affecting the nation as a whole in the longer term. And it has its own unique issues to address.

# **CHAPTER 4**

## **Intercity and High-Speed Rail Service in California**

**Axel Sarkissian**

Axel Sarkissian is a UCLA undergraduate.





When California was admitted to the Union in 1850, it was geographically isolated from the rest of the United States. Moreover, the sheer size of the state made transportation within the state itself an exceedingly difficult task. Until the arrival of the transcontinental railroad in 1869, California was essentially separate from the rest of the United States. That first rail link connected the state's people, economy, and government to the greater United States, proving to be an indispensable tool in the process of making the state into what it is today. The subsequent proliferation of privately constructed and held railroads provided an extensive passenger and freight network, connecting the state's cities to each other and laying the groundwork for the economic powerhouse that the state would become.

Although freight rail remains an important part of California's transportation infrastructure in the modern era, intercity passenger rail operations began to suffer in the 1940s with the development of the state's highways. In the following decades, intercity service dwindled to a bare minimum. The creation of Amtrak on May 1, 1971, ensured the continued survival of intercity passenger service throughout the state, although the rail network has yet to recover the majority of its lost trains. This chapter will provide an overview of the current situation of intercity passenger rail service and outline where the state plans on going next, along with a brief look at the factors that have led to the current condition of intercity rail.<sup>1</sup>

## **History of Intercity Rail in California**

*"The cold fact looms that the long-distance passenger train is dead and no amount of prayer or wishful thinking can bring it back to life."*

Benjamin F. Biaggini, president, Southern Pacific Railroad<sup>2</sup>

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<sup>1</sup>This chapter is based on a term paper originally prepared for Public Policy 10B, California Policy Issues, in Winter 2016.

<sup>2</sup> Solomon, B. (2005). *Southern Pacific Passenger Trains*. St Paul, MN: MBI.

American railroading has a rich and colorful history, and California plays a large role in that story. The arrival of the aforementioned transcontinental railroad launched an era of tremendous infrastructure expansion across the state. Although the particular details far exceed the scope of this chapter, it should be noted that important rail links were built between most major cities in the state in the decades following 1869. These lines, normally built by independent companies (the modern day equivalent of which would be a short line, or Class III, railroad) were largely point-to-point services. As with other industries during this period, expansion was followed by consolidation. The beginning of the 20<sup>th</sup> century saw three major railroads in California—the Southern Pacific (SP), the Atchison, Topeka, and Santa Fe, and the Union Pacific (UP)—which provided extensive intercity passenger and freight service. They also were the state’s largest private landowners.

Throughout California’s history, the state’s railroads have played a crucial part in the state’s economic and social development. Both passenger and freight rail enabled the state’s economy to grow at an outstanding rate. California railroads were particularly notable for their efforts in marketing California to the rest of the United States, encouraging tourism and trade with the state, and demonstrating the importance of intercity connections. However, passenger rail began to suffer as the popularity of passenger vehicles surged.

Following World War II, automobile ownership increased exponentially and the federal government invested millions in highway construction. This tilt toward road-based transportation, paired with the rapid development of passenger aircraft, caused rail ridership to plummet. By 1950, the Southern Pacific was losing \$35.7 million a year operating passenger trains. The situation was similar at other railroads, with UP losing \$30.2 million and the Santa Fe \$20 million. As airlines gained ground, railroad passenger

operations hemorrhaged more money: by 1955, SP had a passenger deficit of \$50.2 million, UP of \$46.2 million, and Santa Fe of \$40.9 million.<sup>3</sup>

While automobiles, buses, and aircraft received millions in government subsidies—through taxpayer-funded construction of roads, airports, air traffic control systems, and other crucial infrastructure—railroads never had such a luxury. The cost of laying down rail, bridge building, tunneling and similar indispensable construction was borne by the railroads themselves. While freight rail continued to be profitable, passenger services became unsustainable; railroads operated crumbling trains at the behest of government regulators, who required service.

By the time the federal government decided to step in, there was very limited rail service in California. Prior to the incorporation of the National Railroad Passenger Corporation (known as Amtrak) in 1971,<sup>4</sup> only the *San Joaquin Daylight*,<sup>5</sup> *Sacramento Daylight*,<sup>6</sup> *San Diegan*,<sup>7</sup> *San Francisco Chief*,<sup>8</sup> *Sunset*,<sup>9</sup> *Cascade*,<sup>10</sup> *Super Chief*,<sup>11</sup> *Coast Daylight*,<sup>12</sup> and *City of Los Angeles*<sup>13</sup> were still in operation,<sup>14</sup> many at less-than-daily frequencies. After its establishment, Amtrak shed all but four of these routes. The Southern Pacific continued to operate the *Peninsula Commute*, a commuter rail service between San Jose and San Francisco,<sup>15</sup> which became state-subsidized in 1980 and was renamed Caltrain. The State of California began its direct involvement in intercity rail in

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<sup>3</sup>Solomon, B. (2005). *Southern Pacific Passenger Trains*. St Paul, MN: MBI.

<sup>4</sup>Kelly, J. (2001, June 5). Amtrak's beginnings. *Classic Trains*. Retrieved from <http://ctr.trains.com/railroad-reference/operations/2001/06/amtraks-beginnings>

<sup>5</sup>SP, Los Angeles – Oakland via the Tehachapi pass

<sup>6</sup>SP, Los Angeles – Sacramento

<sup>7</sup>Santa Fe, Los Angeles – San Diego

<sup>8</sup>UP, Oakland – Chicago

<sup>9</sup>SP, Los Angeles – New Orleans

<sup>10</sup>SP, Oakland – Seattle

<sup>11</sup>Santa Fe, Los Angeles – Chicago

<sup>12</sup>SP, Los Angeles – San Francisco

<sup>13</sup>UP, Los Angeles - Omaha

<sup>14</sup>Edmonson, H. A. (1972). *Passenger Trains Operating on the Eve of Amtrak*. Retrieved from [http://ctr.trains.com/~media/import/files/pdf/f/7/7/passenger\\_trains\\_operating\\_on\\_the\\_eve\\_of\\_amtrak.pdf](http://ctr.trains.com/~media/import/files/pdf/f/7/7/passenger_trains_operating_on_the_eve_of_amtrak.pdf)

<sup>15</sup>Caltrain. (n.d.). *Historic Milestones* [Fact sheet]. Retrieved October 1, 2016, from <http://www.caltrain.com/about/Caltrain150/Milestones.html>

1977, partnering Caltrans, the state's department of transportation, with Amtrak to create Amtrak California.

### **Current Situation**

Amtrak operates the bulk of California's present day intercity rail services, with a smattering of commuter operators providing substantial near-distance service in the Central Valley, Bay Area, and Los Angeles. California's intercity rail system is relatively extensive, with the state commanding about 20 percent of the nation's intercity riders.<sup>16</sup> Currently, there are three intercity lines; all see service multiple times in a day.

The *San Joaquin*, which originates in Bakersfield and serves Oakland four times daily and Sacramento twice daily (on weekdays), is operated with a California Department of Transportation (Caltrans) subsidy of \$31.8 million (as of 2012-13) and had revenue of \$40.8 million on a ridership of 1.1 million in FY 2011-12.<sup>17</sup> In July 2015, management of *San Joaquin* was transferred from Caltrans to the San Joaquin Joint Powers Authority. The Authority is composed of local municipalities and counties that plan on adding an additional roundtrip from Bakersfield to Oakland in mid-2016.

The *Pacific Surfliner*, also branded as an Amtrak California service, is Amtrak's most heavily traveled route outside of the Northeast Corridor.<sup>18</sup> It provides service between San Diego and San Luis Obispo, with ridership hitting a record 2.7 million in FY 2013-14.<sup>19</sup> In FY 2011-12, the train had revenues of \$42.8 million, and received a state subsidy of \$31.6 million. The train's operating authority, the Los Angeles – San Diego – San Luis

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<sup>16</sup>San Joaquin Joint Powers Authority. (2015). *2015 business plan*. Retrieved from <http://www.acerail.com/About/Regional-Governance-for-San-Joaquin-Rail-Service/SJJPA-Bus-Plan-2015-Final.pdf>

<sup>17</sup>San Joaquin Joint Powers Authority. (2015). *2015 business plan*. Retrieved from <http://www.acerail.com/About/Regional-Governance-for-San-Joaquin-Rail-Service/SJJPA-Bus-Plan-2015-Final.pdf>

<sup>18</sup>Los Angeles – San Diego – San Luis Obispo Rail Corridor Agency. (2015, June). *LOSSAN rail corridor agency business plan*. Retrieved from <http://www.octa.net/pdf/LOSSAN%20Business%20Plan%20FINAL.pdf>

<sup>19</sup>Ibid.

Obispo Rail Corridor Agency (LOSSAN), plans to operate (in FY 2015-2016) 24 daily weekday trains between Los Angeles and San Diego, 10 daily trains between Los Angeles and Goleta, and four trains between Los Angeles and San Louis Obispo. This constitutes an increase of service of two trains over FY 2014-2015, the first increase in service on the corridor in over a decade.

The *Capitol Corridor*, operated by Amtrak—but not as an Amtrak California train—sees seven daily weekday roundtrips between San Jose and Oakland and an additional 15 roundtrips between Oakland and Sacramento (one daily train continues to Auburn).<sup>20</sup> In FY 2014-15, the *Capitol Corridor* saw 1.4 million passengers and reported revenues of \$28.4 million.<sup>21</sup> Caltrans allocated \$36.7 million in FY 2014-15 to the Capitol Corridor Joint Powers Authority, which oversees the operation of the line.<sup>22</sup>

All three lines provide frequent, intercity service—and all three lines have posted ridership gains year-over-year (with the exception of the *San Joaquin*, due to a change in rolling stock which resulted in a minor loss in the past fiscal year).<sup>23</sup> These state-supported services demonstrate that there is a strong market for intercity rail travel in California; indeed, all three respective joint powers authorities predict substantial growth for their lines if allocated more equipment and the required funding to operate it. Like all forms of mass transportation—public and private—rail has a substantial positive economic and environmental impact. The performance of intercity trains operated in California proves that people are willing to ride them; it falls on the state and federal governments to improve service and to entice more passengers.

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<sup>20</sup>National Railroad Passenger Corporation. (2013). *Amtrak fact sheet, fiscal year 2013 state of California* [Fact sheet]. Retrieved February 25, 2016, from <https://www.amtrak.com/pdf/factsheets/CALIFORNIA13.pdf>

<sup>21</sup>Capitol Corridor Joint Powers Authority. (2015, April 10). *CCJPA FY 2015-16 – FY 2016-17 business plan update*. Retrieved from [http://www.capitolcorridor.org/included/docs/business\\_plans/FY-2015-16-FY-2016-17.pdf](http://www.capitolcorridor.org/included/docs/business_plans/FY-2015-16-FY-2016-17.pdf)

<sup>22</sup>*Ibid.*

<sup>23</sup>San Joaquin Joint Powers Authority. (2015). *2015 business plan*. Retrieved from <http://www.acerail.com/About/Regional-Governance-for-San-Joaquin-Rail-Service/SJJPA-Bus-Plan-2015-Final.pdf>

## Long-Distance Trains

In addition to these services, Amtrak operates four long-distance trains—*Southwest Chief*,<sup>24</sup> *Sunset Limited*,<sup>25</sup> *California Zephyr*,<sup>26</sup> and *Coast Starlight*<sup>27</sup>—in California, although only *Coast Starlight* provides meaningful inter-state service. These four trains are a cornerstone of Amtrak’s national long distance system, which is supported by federal funds. While the *Southwest Chief*, *Sunset Limited*, and *California Zephyr* provide important services to California, they call at few stations within the state and thus their operation is beyond the scope of this chapter.

The *Coast Starlight* serves 16 communities between Los Angeles and Dunsmuir, providing the only rail connection between southern and northern California. The trip between Los Angeles and Oakland takes 11 hours. Between Los Angeles and Sacramento it takes 13 hours. (Both northbound and southbound trains depart Sacramento at difficult hours.) Between Los Angeles and Dunsmuir, travel time is 16 hours.<sup>28</sup> (The train calls Dunsmuir in the very early hours of the morning in both directions).

The sole north-south rail link in the state has a decidedly unattractive schedule that disfavors inter-state travel in meaningful numbers and discourages anything but leisure and cost-sensitive traffic. To be effective and sustainable, public transportation must attract a wide cross section of traffic. Business travelers are arguably the most important, as they constitute a large portion of overall traffic between any two cities and are the least cost-sensitive.

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<sup>24</sup>Los Angeles – Chicago, daily

<sup>25</sup>Los Angeles – New Orleans, thrice weekly (two cars transfer at San Antonio to *Texas Eagle*, with service to Chicago)

<sup>26</sup>Emeryville – Chicago, daily

<sup>27</sup>Los Angeles – Seattle, daily

<sup>28</sup>Amtrak. (2016). *Coast Starlight schedule* [Pamphlet]. Retrieved from <https://www.amtrak.com/ccurl/800/746/Coast-Starlight-Schedule-011116.pdf>

## Commuter Services

There are three commuter rail services in California which run trains that connect several cities. Caltrain operates 92 weekday trains over the San Francisco – Gilroy line, and recorded a ridership of 18.5 million passengers in FY 2014.<sup>29</sup> Metrolink operates 165 trains each weekday over seven lines in five counties in Southern California, with a ridership of nearly 5.8 million in FY 2016.<sup>30</sup> Additionally, the Altamont Corridor Express operates four trains a day between Stockton and San Jose with an annual ridership of 1.3 million.<sup>31</sup> These operators provide crucial services for the areas that they serve, and cannot be overlooked when examining the state’s plan for rail. However, because their impact is highly localized, they are not the focus of this chapter.

## State Policy Toward Rail

When compared to other states, California’s passenger rail system is fairly developed. Sacramento has demonstrated strong support for intercity rail across the state (Amtrak California funding exceeds \$90 million a year). The state’s support is justified; California’s intercity rail system has high ridership numbers and grows more popular every year. However, there is potential for major growth in conventional heavy rail service. Note that current ridership numbers persist in spite of the inefficiencies, bad scheduling, old equipment and second rate infrastructure which plagues passenger train service in California (and the greater United States).

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<sup>29</sup>Caltrain. (n.d.). *Ridership* [Fact sheet]. Retrieved February 25, 2016, from <http://www.caltrain.com/about/statsandreports/Ridership.html>

<sup>30</sup>Metrolink. (2016, January). *Metrolink fact sheet Q1 2016* [Fact sheet]. Retrieved February 25, 2016, from [http://www.metrolinktrains.com/pdfs/Facts&Numbers/Fact\\_Sheets/Fact\\_Sheet\\_2016\\_Q1.pdf](http://www.metrolinktrains.com/pdfs/Facts&Numbers/Fact_Sheets/Fact_Sheet_2016_Q1.pdf) and Metrolink. (2016, January). *Metrolink ridership* [Fact sheet]. Retrieved February 25, 2016, from [http://www.metrolinktrains.com/pdfs/Facts&Numbers/Monthly\\_Line\\_Ridership/Average\\_and\\_Total\\_Ridership\\_Report\\_FY16.pdf](http://www.metrolinktrains.com/pdfs/Facts&Numbers/Monthly_Line_Ridership/Average_and_Total_Ridership_Report_FY16.pdf)

<sup>31</sup>Leavitt, D. (2015, July 23). *Improving the Altamont Corridor Express*. Retrieved from [https://www.acerail.com/About/PublicProjects/ACEforward/ACEforward\\_July2015-email-web.pdf](https://www.acerail.com/About/PublicProjects/ACEforward/ACEforward_July2015-email-web.pdf)



In the past several years, the state has invested heavily in capital projects, with \$44.9 million earmarked for Capitol Corridor improvements alone.<sup>32</sup> These measures include federally mandated safety features such as positive train control in addition to other improvements. The state's legislature has become more receptive to rail, recently forming select committees on passenger rail in both chambers.<sup>33</sup> Utilizing funds from California's cap and trade auctions, Senate Bill 862 established the California Gas Reduction Fund, which allows the three passenger rail lines and their respective joint powers authorities to apply for capital funding.

In addition, the widespread positive impact of passenger rail on other sectors has fueled new support, inside government and out, for intercity service. One of the current administration's policy priorities is environmental sustainability, which benefits strongly from rail. An estimated total of 109 million pounds of CO<sup>2</sup> emissions and 355 million road miles are eliminated annually due to the operation of the *Capitol Corridor*, *San Joaquin*, and *Pacific Surfliner*.<sup>34</sup> Any increase of service on current lines and a potential expansion of the network would only increase these numbers.

Additionally, the economic impact of rail is large, albeit difficult to quantify. Thousands of jobs are directly supported by rail operations, and many more could benefit if new capital projects were undertaken by the state. The first stage of high-speed rail, which began construction in 2014, is said to have created about 20,000 jobs annually although one must often be cautious about claimed "multiplier" estimates.<sup>35</sup> It is important to note that railroad jobs are, by any standard, good work. Average wages and benefits

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<sup>32</sup>San Joaquin Joint Powers Authority. (2015). *2015 business plan*. Retrieved from <http://www.acerail.com/About/Regional-Governance-for-San-Joaquin-Rail-Service/SJIPA-Bus-Plan-2015-Final.pdf>

<sup>33</sup>Caltrans. (2015, April). *Connecting cities, connecting regions, connecting people: California's intercity passenger rail program*. Retrieved from <http://www.octa.net/pdf/CAIPRBrochure.pdf>

<sup>34</sup>Ibid.

<sup>35</sup>California High-Speed Rail Authority. (2015, April). *Creating Jobs Through High-Speed Rail* [factsheet]. Retrieved from [https://www.hsr.ca.gov/docs/newsroom/fact%20sheets/Jobs\\_Factsheet\\_FINAL\\_040915.pdf](https://www.hsr.ca.gov/docs/newsroom/fact%20sheets/Jobs_Factsheet_FINAL_040915.pdf)

exceed \$100,000.<sup>36</sup> Pensions are guaranteed through the federal Railroad Retirement Board.

While there is substantial opposition to high-speed rail proposals (covered in detail in a later section), there has been a broad consensus built around conventional heavy rail. Because the state is directly responsible for supporting intercity passenger rail in California, the three major lines can be considered stable for the long term. In addition, while the *Coast Starlight* relies solely on the federal government's funding of Amtrak, long distance trains have very solid support among local populations (and state governments). Simply put, if eliminating the *Coast Starlight* or any other long distance Amtrak train was politically feasible, it would have been done a long time ago.

Although Amtrak is one of Capitol Hill's favorite punching bags, it is highly unlikely that it will be done away with anytime soon. The latest funding bill passed by Congress, Fixing America's Surface Transportation (FAST), included \$10 billion in Amtrak funding over the next five years.<sup>37</sup> One can confidently say that California's long distance trains and the communities they serve are protected from the federal government's budgetary woes, at least in the medium term.

### **Potential Expansion of Service & Gaps in the Network**

High ridership numbers continue to substantiate the clear demand for comprehensive intercity rail in California. Ridership could be pushed higher by operating more trains on existing services—something which, on most lines, is physically impossible due to lack of equipment, infrastructure, host railroad problems, or combinations thereof. The intercity rail network itself, however, leaves much to be desired in its current state.

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<sup>36</sup>Association of American Railroads. (n.d.). U.S. Freight Railroad Industry Snapshot: California. Retrieved from <https://www.aar.org/data-center/railroads-states#state/CA>

<sup>37</sup>Laing, K. (2016, February 16). Amtrak requests \$1.8B for fiscal 2017. *The Hill*. Retrieved from <http://thehill.com/policy/transportation/269711-amtrak-requests-18b-for-2017-fiscal-year>

The most obvious gap is the lack of a connection between Bakersfield and Los Angeles Union Station for the *San Joaquin* service, which is due to the single track at Tehachapi Pass—one of the busiest freight corridors in the U.S.—and Union Pacific’s refusal to allow passenger trains to operate over it. As is the case with other such gaps in the network, passengers are directed to Amtrak Thruway bus services which, although providing an essential service, are a poor substitute for rail between major cities.

The development of high-speed rail will be discussed below. But an integral part of the proposed high-speed corridor includes bridging the gap between Union Station and Bakersfield. Construction, however, is dependent on future federal and state funding that cannot be adequately projected at this point in time. Some interest groups pushed for the Bakersfield-Los Angeles line to be the first step in HSR construction, thus assuring that the line would be open for conventional rail, regardless of HSR’s uncertain future.<sup>38</sup> Despite these efforts, Stage I funding ultimately went elsewhere. As of this writing, there is no concrete timetable for construction of this crucial rail segment—undoubtedly the most important network omission in the state.

Another useful step would be the reestablishment of a *Coast Daylight* service (a former SP train eliminated by Amtrak in 1974).<sup>39</sup> Resumption of that train would serve as a *de facto* extension of the *Pacific Surfliner* by continuing from San Louis Obispo to San Francisco and would provide immediate benefit to those seeking an alternative route between the state’s two largest cities. Caltrans’ current plan—which is far from being a certainty—would see two daily trains by 2020.<sup>40</sup> Although the service would be slow, mirroring that of the *Coast Starlight*, there is little question that demand exists among leisure and price conscious travelers. If the Los Angeles-Bakersfield gap were to be filled,

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<sup>38</sup>Mills, J. R., & Tolmach, R. F. (2011, January). Fill the Bakersfield Gap First. *California Rail News*, 22(1). Retrieved from [http://calrailfoundation.org/HSR\\_files/bakersfieldgap.pdf](http://calrailfoundation.org/HSR_files/bakersfieldgap.pdf)

<sup>39</sup>Caltrans. (2015, April). *Connecting cities, connecting regions, connecting people: California's intercity passenger rail program*. Retrieved from <http://www.octa.net/pdf/CAIPRBrochure.pdf>

<sup>40</sup>Caltrans. (2015, April). *Connecting cities, connecting regions, connecting people: California's intercity passenger rail program*. Retrieved from <http://www.octa.net/pdf/CAIPRBrochure.pdf>

travel time between Los Angeles and San Francisco could decrease exponentially with some alterations to routes and schedules.

There is one new line that is the subject of a comprehensive feasibility study being undertaken by Caltrans and the FRA.<sup>41</sup> The current proposal is a Los Angeles-Coachella Valley line, which would run through parts of the Imperial Valley and into San Bernardino. Both these areas are heavily populated, but lack access to the intercity rail system; their relative proximity to Los Angeles would make this service a valuable one for commuters. Another proposal currently being studied is an extension of *Capitol Corridor* to Salinas, linking the large population center to the rest of the line. The implementation of the *Coast Daylight*, the Coachella Valley line, and the *Capitol Corridor* extension are estimated to carry up to 400,000 passengers annually.<sup>42</sup>

### **Infrastructure and Equipment**

Railroads are inherently infrastructure-intensive. Although Caltrans and the commuter operators would like to increase frequencies on their lines, they simply do not have the rolling stock to do so. The state has allocated \$150 million on top of a \$168 million contribution from the federal government to purchase 51 passenger cars and 21 locomotives, due to be delivered in 2017.<sup>43</sup> It is important to underline the unique situation in which California operates its rail system: Caltrans owns the cars and engines, while Amtrak operates the trains. This separation of responsibility means that the state is solely responsible for securing the railcars utilized.

Both the *San Joaquin* and the *Capitol Corridor* utilize California Cars, which are bi-level coaches. The *Surfliner* operates updated California Cars dubbed Surfliners. Chronic

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<sup>41</sup>Riverside County Transportation Commission. (2015, October). *Coachella Valley-San Geronio Pass Corridor Rail Service Study*. Retrieved from <http://rctcftp.org/files/PwgrG-MbbQM=/2.A1.RY.Executive%20Summary%20from%20the%20draft%20alt%20analysis%2010%2014.pdf>

<sup>42</sup>Caltrans. (2015, April). *Connecting cities, connecting regions, connecting people: California's intercity passenger rail program*. Retrieved from <http://www.octa.net/pdf/CAIPRBrochure.pdf>

<sup>43</sup>Caltrans. (2015, April). *Connecting cities, connecting regions, connecting people: California's intercity passenger rail program*. Retrieved from <http://www.octa.net/pdf/CAIPRBrochure.pdf>

equipment shortages have led Amtrak to source one single-level Amfleet consist from its East Coast operations for operations on the *Surfliner*. Additionally, Caltrans recently purchased 14 Comet IB coaches from New Jersey Transit, which Amtrak refurbished at its Beech Grove shops.<sup>44</sup> In conjunction with a Horizon café car, they operate on the *San Joaquin* in five car consists. While the cars are a cost-effective stopgap, they are indicative of the larger problem facing the state: Caltrans suffers from a serious equipment shortage. And although 51 new bi-level cars are on the way, the added capacity still will not be enough to increase services on current lines while simultaneously expanding the state's network.

The state's infrastructure situation is not much better. Much of it is either outdated or is not suited to passenger operation. Investment in signaling improvements and track work is necessary, and Caltrans has been moving forward with capital projects focusing on such corridor improvements. A key component to reducing travel times—crucial to increase the attractiveness of the service—is track improvements. However, because speed is not a priority for freight railroads, there is little will on their part to spend money on non-essential track work. As the state does not own the rail over which trains operate, its ability to undertake improvements is limited.

## High Speed Rail

California has long been identified as an ideal candidate for the implementation of high-speed rail in the United States. Currently, the only high-speed rail system in North America is Amtrak's *Acela Express*, which operates between Washington, D.C. and Boston on the Northeast Corridor. It reaches its top speed of 150 miles per hour on roughly 30 miles of track out of the route's 226-mile total.<sup>45</sup> Studies of a potential high-

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<sup>44</sup>Brinckerhoff, P. (2012, August 30). *Caltrans Comet IB presentation to the San Joaquin Valley rail committee* [PowerPoint slides]. Retrieved February 25, 2016, from [http://149.136.20.80/rail/dor/assets/File/August\\_30.2012/Caltrans\\_Comet\\_IB\\_SJVRC\\_Presentation\\_-\\_08.27.12-B.Tsukamoto.pdf](http://149.136.20.80/rail/dor/assets/File/August_30.2012/Caltrans_Comet_IB_SJVRC_Presentation_-_08.27.12-B.Tsukamoto.pdf)

<sup>45</sup>National Association of Railroad Passengers. (2013). *Amtrak fact sheet: Acela service*. Retrieved from <http://narprail.org/site/assets/files/1038/trains.pdf>

speed rail corridor in California began in the late 1980s.<sup>46</sup> Planning began in earnest with the creation of the California High-Speed Rail Authority by the legislature in 1996.<sup>47</sup> The current plan would see Los Angeles and San Francisco linked together by 2029, with trains operating over 200 miles per hour for a total journey time of under three hours.<sup>48</sup>

In 2008, California voters approved Proposition 1A, authorizing a \$9.95 billion bond issuance for the construction of a high-speed rail corridor. As part of the federal response to the Great Recession of 2008-09, the state received an additional \$3.3 billion in American Recovery and Reinvestment Act (ARRA) stimulus funding for the project in 2009. Phase I—Los Angeles to San Francisco—has an estimated price tag of \$68.4 billion.<sup>49</sup> Revenue from the state's cap and trade program, currently benefiting conventional rail services, will be repurposed and utilized to fund construction of the corridor.

Additionally, the California High-Speed Rail Authority has planned Phase II of the project, although it lacks a timetable for completion. This phase would see the corridor extended in the north from Merced to Sacramento and in the south from Anaheim to San Diego. Construction has begun in the Central Valley between Merced and Bakersfield; completion is expected in 2018.<sup>50</sup> Although high-speed trains will not yet run on this line, the aforementioned *San Joaquin* service will be able to operate at much higher speeds. By 2022, the line between Burbank and Merced should be completed and operating.<sup>51</sup> The year 2027 should see trains running between Los Angeles Union

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<sup>46</sup>California High-Speed Rail Authority. (2014, May 1). *Connecting California: 2014 business plan*. Retrieved from [http://www.hsr.ca.gov/docs/about/business\\_plans/BPlan\\_2014\\_Business\\_Plan\\_Final.pdf](http://www.hsr.ca.gov/docs/about/business_plans/BPlan_2014_Business_Plan_Final.pdf)

<sup>47</sup>Ibid.

<sup>48</sup>California High-Speed Rail Authority. (2014, May 1). *Connecting California: 2014 business plan*. Retrieved from [http://www.hsr.ca.gov/docs/about/business\\_plans/BPlan\\_2014\\_Business\\_Plan\\_Final.pdf](http://www.hsr.ca.gov/docs/about/business_plans/BPlan_2014_Business_Plan_Final.pdf)

<sup>49</sup>Nash, J. (2015, October 19). Banks may balk at financing \$68 billion California bullet train. *Bloomberg Business*. Retrieved February 25, 2016, from <http://www.bloomberg.com/news/articles/2015-10-19/banks-may-balk-at-financing-68-billion-california-bullet-train>

<sup>50</sup>California High-Speed Rail Authority. (2014, May 1). *Connecting California: 2014 business plan*. Retrieved from [http://www.hsr.ca.gov/docs/about/business\\_plans/BPlan\\_2014\\_Business\\_Plan\\_Final.pdf](http://www.hsr.ca.gov/docs/about/business_plans/BPlan_2014_Business_Plan_Final.pdf)

<sup>51</sup>Ibid.

Station and San Francisco Transbay Transit Center; between Los Angeles and San Jose, trains will run on dedicated HSR track.<sup>52</sup>

The primary hurdle that California high-speed rail faces is cost. The high price tag is enough to scare off many potential political supporters; several missteps during 2016 by CHSRA eroded confidence in the organization, even among its supporters. Although critics have long insisted that cost overruns are unavoidable, CHSRA officials repeatedly stated that contracts currently being executed were below budget. In a February 2016 State Assembly committee hearing, they testified that the cost of the system would not increase. Less than a month afterwards, however, the Authority's consulting firm reported that the price tag for the current construction had risen by five percent—about \$260 million. This admission served to make concrete political opposition to the program, with some members of the Assembly arguing that CHSRA were either incompetent or liars.<sup>53</sup>

CHSRA is obligated to draft a business plan every fiscal year that details every facet of the agency's operation. The 2016 business plan contained a major change from years past. Instead of connecting the construction currently underway in the Central Valley to the San Fernando Valley (thus linking Bakersfield and Los Angeles), the agency has decided to build the line out to San Jose.<sup>54</sup> The terminus in the Central Valley would become the City of Shafter, roughly 50 miles away from any previously planned station. The agency cited the lesser engineering challenges—and, in turn, costs—in construction of this segment.

California's Legislative Analyst's Office (LAO) reviewed the 2016 business plan and was sharply critical of several components, including the proposed realignment of

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<sup>52</sup>California High-Speed Rail Authority. (2014, May 1). *Connecting California: 2014 business plan*. Retrieved from [http://www.hsr.ca.gov/docs/about/business\\_plans/BPlan\\_2014\\_Business\\_Plan\\_Final.pdf](http://www.hsr.ca.gov/docs/about/business_plans/BPlan_2014_Business_Plan_Final.pdf)

<sup>53</sup>Vartabedian, R. (2016, February 16). Cost of California bullet train's Central Valley leg projected to grow by \$260 million. *Los Angeles Times*. Retrieved from <http://www.latimes.com/local/california/la-me-bullet-overruns-20160217-story.html>

<sup>54</sup>California High-Speed Rail Authority. (2016, May 1). *Connecting and Transforming California: 2016 business plan*. Retrieved from [http://www.hsr.ca.gov/docs/about/business\\_plans/2016\\_BusinessPlan.pdf](http://www.hsr.ca.gov/docs/about/business_plans/2016_BusinessPlan.pdf)

resources.<sup>55</sup> LAO noted that ending the line “in an unpopulated agricultural area does not appear to be an effective approach.”<sup>56</sup> It also underlined the lack of specificity in CHSRA’s business plan. LAO complained that the agency was changing the scope and requirements for projects over time and thus making oversight of budget expenditures by the legislature difficult. Moreover, while CHSRA projected nearly \$150 million in funds stemming from the state’s cap and trade auction in May 2016, it actually received only \$2.5 million.<sup>57</sup> This shortfall of funding casts CHSRA’s future revenue projections into doubt, especially as cap and trade has long been touted as a key funding source for the project.

If the HSR system is to be completed, it will require a substantial capital investment from the state and from the federal government. While the Obama administration has supported high-speed rail, federal investment for projects such as California’s remains highly uncertain in the long term. The chairman of the House Railroads, Pipelines and Hazardous Materials Subcommittee, Jeff Denham of California’s 10<sup>th</sup> congressional district, is a staunch opponent of California’s high-speed rail program. If constructed, the high-speed rail line would run right through the middle of his largely rural district, with a stop in Modesto.

Representative Denham favors strong investment in passenger rail—his committee passed, with broad bipartisan support, the Passenger Rail Reform and Investment Act (PPRIA) which appropriates billions for rail passenger infrastructure. However, he has deemed California’s HSR project a “disaster.”<sup>58</sup> Because federal funds are undoubtedly

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<sup>55</sup>California Legislative Analyst's Office. (2016, March 17). *Review of High-Speed Rail Draft 2016 Business Plan* (M. Taylor, Author).

Retrieved from <http://www.lao.ca.gov/reports/2016/3394/HSR-Draft-Business-Plan-Review-031716.pdf>

<sup>56</sup>Ibid.

<sup>57</sup>Vartarbedian, R.. (2016, May 25). State cap-and-trade auction falls far short, hurting bullet train. *Los Angeles Times*. Retrieved from

<http://www.latimes.com/local/california/la-me-cap-trade-20160525-snap-story.html>

<sup>58</sup>Office of Rep. Denham. (2015, March 4). House Passes Passenger Rail Reform and Investment Act [Press release]. Retrieved from <https://denham.house.gov/media-center/press-releases/%20house-passes-passenger-rail-reform-and-investment-act>



necessary for construction of the system, the opposition from the top House Republican on railroads is an important factor to consider when examining the long-term viability of the HSR system.

In short, at the federal level, the future of true HSR in California is by no means certain. Although federal investment in the system would best be characterized as a drop in the bucket when compared with the rest of the federal budget, fundamental opposition from Republican members of the House makes any debate regarding the issue futile. However, increased investment in corridor modernization (signaling, track work, and so on) to improve conventional rail speeds is likely to find continued support in Congress.

Future support at the state level is also uncertain. Although he was an early HSR supporter, Lieutenant Governor Gavin Newsom—a candidate for governor in 2018—has expressed his opposition to the project. He argues that the project presented to voters in 2008 is very different from the current plan. Additionally, Newsom cites the uncertainty of federal dollars, price increases, and constant delays as reasons to oppose the project.<sup>59</sup> He also claims that other Democrats in the state government feel the same way, but do not comment publicly.

The degree to which state Democrats silently oppose the HSR is hard to gauge. But Democratic Representative Mark DeSaulnier, former chair of the Transportation Committee in the state Senate, has agreed with Newsom's comments.<sup>60</sup> Elsewhere in the state, the situation is similar. Kevin Faulconer, the popular moderate Republican mayor of San Diego is skeptical of HSR.<sup>61</sup> At this writing, he has indicated a lack of interest in the gubernatorial race, but hasn't entirely pulled out. On the other hand, former Los Angeles mayor Antonio Villaraigosa, a prominent Democrat mulling a run for

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<sup>59</sup>Marinucci, C. (2014, February 19). California high-speed rail dealt blow by Newsom's about-face. *San Francisco Chronicle*. Retrieved from <http://www.sfgate.com/politics/article/California-high-speed-rail-dealt-blow-by-Newsom-s-5246249.php>

<sup>60</sup>Ibid.

<sup>61</sup>Nichols, C. (2014, November 2). Hurry up, wait for high-speed rail. *San Diego Union Tribune*. Retrieved from <http://www.sandiegouniontribune.com/news/2014/nov/02/high-speed-rail-bullet-train-san-diego/>

governor, is supportive of high-speed rail.<sup>62</sup> And current state treasurer, Democrat John Chiang, has not expressed his opinion either way on the issue.

At this writing, there is a lack of strong public support for the project. Proposition 1A, which launched the HSR project in the state, passed in 2008 with 52% support.<sup>63</sup> A subsequent Public Policy Institute of California poll in 2016 found that 52% of Californians (but 44% of likely voters) were in favor of the project.<sup>64</sup> Cost seems to be the primary concern of the electorate. When asked how they would feel if HSR were cheaper, 66% of respondents said they would be in favor of the project. Central Valley voters, however, who would be the first to benefit from HSR, opposed the project by 53% to 44%. The scope and expense of the project, coupled with its lukewarm reception by the public, puts HSR's future decidedly in doubt, particularly after the final term of Governor Jerry Brown, who championed the project.

In late September 2016, Governor Brown signed AB 1889.<sup>65</sup> The legislation made Proposition 1A funds available for bookend commuter railroad improvements.<sup>66</sup> This funding—over a billion dollars—is intended for electrification work to be undertaken on the Caltrain system.<sup>67</sup> It will also allow future work to be done in the Los Angeles area by Metrolink and the Los Angeles County Metropolitan Transportation Authority in preparation for the arrival of HSR. AB 1889 had opposition from Democrats, who argued

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<sup>62</sup>Finnigan, M. (2015, April 26). Villaraigosa: Democrats stuck in past, Clinton faces tight race. *The Los Angeles Times*. Retrieved from <http://www.latimes.com/local/political/la-me-pc-villaraigosa-clinton-president-20150424-story.html>

<sup>63</sup>Baldassare, M., Bonner, D., Kordus, D., & Lopes, L. (2016, March). *Californians & Their Government*. San Francisco, CA: Public Policy Institute of California. Retrieved from [http://www.ppic.org/content/pubs/survey/S\\_316MBS.pdf](http://www.ppic.org/content/pubs/survey/S_316MBS.pdf)

<sup>64</sup>Ibid.

<sup>65</sup>California Legislative Information. (2016, September 29). *AB-1889 High-Speed Rail Authority: high-speed train operation* [Bill Tracker]. Retrieved from [https://leginfo.ca.gov/faces/billStatusClient.xhtml?bill\\_id=201520160AB1889](https://leginfo.ca.gov/faces/billStatusClient.xhtml?bill_id=201520160AB1889)

<sup>66</sup>Bollag, S. (2016, August 31). Bill to advance California's high-speed rail project is sent to Gov. Brown. *The Los Angeles Times*. Retrieved from <http://www.latimes.com/politics/essential/la-pol-sac-essential-politics-updates-bill-to-advance-high-speed-rail-project-1472711275-htmlstory.html>

<sup>67</sup>Associated Press. (2016, September 1). California Assembly Approves \$1.1 Billion To Electrify Caltrain. *CBS Bay Area*. Retrieved from: <http://sanfrancisco.cbslocal.com/2016/09/01/california-assembly-approves-1-1-billion-to-electrify-caltrain/>

that HSR was Balkanizing into regional projects, and Republicans, who said the voters' intentions in 2008 had been ignored.<sup>68</sup>

Concurrent with signing AB 1889, Brown vetoed AB 2847,<sup>69</sup> which had passed both houses of the legislature unanimously.<sup>70</sup> It incorporated several of the LAO's recommendations following its analysis of CHSRA's business plan. AB 2847 would have required the CHSRA to provide scope and cost information for individual segments of the project and to detail the sources of funding for each segment. The bill's veto, especially considering the wide political support it enjoyed, made the longer term political future of HSR in Sacramento even more uncertain.

## Conclusion

California has a storied relationship with railroads. From the first trains that rolled into the state in 1869 to the heavily trafficked corridors today, intercity train transportation has played a crucial role in the development of the state's economy and society.

Although long distance services have suffered greatly and continue to do so, intercity rail has experienced a resurgence in the past decades. The continued development of the *San Joaquin*, *Capitol Corridor*, and *Pacific Surfliner*, and the state's commitment to increase service on those lines, are a crucial advancement in California's transportation policy.

There are several pressing needs that must be addressed by both the state and the federal government. As with any transportation system, the priority will always be increasing ridership. To achieve this goal, the first—and most important—policy focus

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<sup>68</sup>Vartarbedian, R.. (2016, July 30). New political and legal battle is shaping up for California bullet train. *Los Angeles Times*. Retrieved from <http://www.latimes.com/local/la-me-bullet-train-battle-20160729-snap-story.html>

<sup>69</sup>Vartarbedian, R.. (2016, September 28). New political and legal battle is shaping up for California bullet train. *Los Angeles Times*. Retrieved from <http://www.latimes.com/local/california/la-me-bullet-oversight-veto-20160928-snap-story.html>

<sup>70</sup>California Legislative Information. (2016, September 29). *AB-2847 High-Speed Rail Authority: reports*. [Bill Tracker]. Retrieved from [https://leginfo.ca.gov/faces/billVotesClient.xhtml?bill\\_id=201520160AB2847](https://leginfo.ca.gov/faces/billVotesClient.xhtml?bill_id=201520160AB2847)

must be the improvement of existing rail infrastructure. Existing corridors, the *Coast Starlight*, and commuter rail would all greatly benefit from advances in this area, which would allow more trains to run in a safer manner and at higher speeds. Capital investment in infrastructure is a prerequisite for any other action that the state may be inclined to take; even with current network gaps, faster and more frequent trains are the primary way to drive passenger growth.

Additionally, there is the important matter of patching holes in the network. A rail link between Bakersfield and Los Angeles ought to be the first priority for the state, although the current situation with Union Pacific makes that almost impossible. While the state is focusing on the construction of a high-speed rail link between the two cities, that branch of HSR remains unfunded and its future is unknown. Still, every effort must be made to extend the *San Joaquin* to Los Angeles Union Station.

Both the operation of a twice-daily *Coast Daylight* service and the start of the planned Coachella Valley line would constitute crucial additions to the state's passenger rail network and would increase the long-term viability of passenger rail as an alternative to the automobile. However, state investment in additional rolling stock would be required. The existing shortage of both engines and passenger cars make any increase in service—let alone the launch of new routes—impossible.

Although the construction of a true HSR corridor in California would prove to be a watershed moment in North American public transportation, high-speed rail does not have a stable future in the state. There is substantial opposition to the project by important figures in both political parties at the state level, including among likely gubernatorial candidates. At the federal level, opposition to the program from the top House Republican on railroads makes further federal funding uncertain.

If money were to be appropriated, the best course of action would be to bridge the Bakersfield-Los Angeles gap first. But if funding for true HSR cannot be secured, then further investment in conventional rail infrastructure with the goal of increasing speeds

ought to be the state's goal. In any event, CHSRA appears to be moving away from the gap in southern California by planning on constructing the link to San Jose first.

California's railroads—both passenger and freight—have always been one of the primary drivers of the state's social and economic development. Their importance in the economic advancement of the state is indisputable. Nevertheless, the golden age of train travel—when inexpensive alternative modes of transportation were not available—is long gone, and it will never return. But in the 21<sup>st</sup> century, passenger rail must hold a different but equally important place in the state's economy.

In the past several decades, California has slowly built a capable intercity rail system that carries tens of millions of passengers a year. It now falls upon the state to take the system to the next step. At the most fundamental level, increased capital expenditures in infrastructure and rolling stock, paired with good route planning, can transform the state's rail system into a comprehensive network that will serve the transportation needs of California.

# **CHAPTER 5**

## **What's Wrong with Los Angeles and What Could Fix It?**

**Matthew P. Drennan**

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The best single measure of the economic health of metropolitan areas is per capita personal income. And the best measure of their relative performance is their ranking by that measure. In 1969 Los Angeles ranked 10<sup>th</sup> among U.S. metropolitan areas, San Francisco ranked third and San Jose ranked 8th. In the most recent year, 2014, San Francisco ranked fifth, San Jose ranked third but Los Angeles ranked 29<sup>th</sup>. In that same long period Boston moved from below Los Angeles (28<sup>th</sup> place for Boston) to well above Los Angeles (sixth place for Boston). (Bureau of Economic Analysis 2016)

What happened? What went wrong for Los Angeles? Was location in California a disadvantage over that long period? Evidently not, because San Francisco and San Jose were among the top 10 for that entire period. This paper addresses barriers to economic development thrown up by the city and/or the county, barriers that could be dismantled with much gain for all parties. Also considered are actual or possible economic development programs of the City and County of Los Angeles that are proven failures in the urban development literature and which should be dropped from use or consideration.

### **Loss of Good Jobs**

The deindustrialization that hit eastern and Midwestern cities beginning in the 1960s came much later to Los Angeles but with powerful negative effects. Aerospace and defense industry employment, long the leading manufacturing activities of the Metropolitan Statistical Area (MSA), suffered deep decline beginning in the 1970s. As aerospace and defense jobs disappeared along with related manufacturing, entertainment jobs expanded, becoming the leading industry of the MSA. But compensation of all entertainment workers, stars and gophers, averaged only \$41,000 per year in 2011 compared with \$71,000 for manufacturing.

The new century has not brought a reprieve for the Los Angeles MSA economy. Table 1 summarizes the grim picture. All industries are sorted into losers (job loss in expansions as well as in contractions), winners (job gains in both expansions and contractions), and the cyclical (gains in expansions, losses in contractions). The mix of losers, winners and cyclical adds up to MSA employment in 2011 of 7.4 million, which is 400,000 below the 2007 peak and about the



same as the 2001 total. The industries that comprise the losers had an annual average wage of over \$80,000 while the winners' was not quite \$45,000. With job contractions concentrated in high-wage industries, and job expansions concentrated in low-wage industries, the continuing relative drop in Los Angeles' per capita income position among metro areas is not surprising.

### **Influx of Low-Skilled Immigrants**

A large demographic shift over the past four decades has raised the metro area's share of poorly educated Hispanics from rural areas of Mexico and Central America and reduced its share of highly educated whites and African Americans. As a consequence the human capital share, measured by the percent of adults with at least a college education, is falling behind other metro areas. In 2014, 32 percent of adults in the Los Angeles MSA had bachelor's degrees or higher, identical to the national share.

That figure, however, is far below the share in large booming metro areas of San Jose (47 percent), San Francisco (45 percent), and Boston (43 percent). The New York MSA, with as large a share of immigrants as Los Angeles, has a higher share of educated adults (36 percent). (U.S. Census 2016) This contrast in part reflects that immigrants to New York on average are more educated than immigrants to Los Angeles.

There is not much that local governments can do to counter national structural economic change such as deindustrialization or immigration trends. But educational attainment is a long-term goal local government can pursue, although in the Los Angeles case the separation of the school districts from other local governments is a complication. In any event, it is not clear how to raise educational attainment in a fluid society. Urban economic development is not easy to achieve in part because the power of local government to control or guide economic development is circumscribed. Booms and busts are not subject to local government management. Perhaps the best it can do is to remove barriers.

## **Imagined Barriers to Economic Development in Los Angeles**

Barriers to economic development are identified by some politicians and business leaders as any regulation or tax that business finds burdensome. They contend naively that abolishing clean water restrictions, air pollution standards, worker compensation taxes, and so on would precipitate a burst of private sector investment that would hurtle the urban area onto a high plain of prosperity and job growth. However, evidence-based research and data have debunked that dream: low taxes and deregulation are not a sure route to prosperity. (Meyer 1995; Bartik, undated; Hansen & Kalambokidis 2010)

Figure 1 shows that of five California cities, San Francisco had by far the largest local tax burden per capita in 2010-2011: over \$2,000. The other cities were slightly above or below \$500. Yet San Francisco is not suffering economically. The high-income metro areas are in fact well known for high taxes, strict environmental regulations, and strong labor protections. All are cases of successful economic development. None have achieved that success through low taxes and deregulation.

Environmental restrictions are not barriers to urban economic growth. One careful evidence-based study (Meyer 1995) of environmental regulations in 50 states over two periods posed this question: Do states with stricter environmental policies pay a price in job growth, and if so, how much?

The study concluded that there was no systematic relationship, positive or negative, between state environmental policies and state economic performance in good economic times. However, it was found that in recessions, stronger environmental policies were associated with weaker economic performance. Nonetheless, over the long term, environmental deregulation cannot be expected to produce measurable economic benefits. In short, the strict air quality laws of California and the County of Los Angeles do not seem to pose a barrier to economic development. Indeed it is doubtful that households and businesses in Los Angeles would be as tolerant today as they were in the 1960s of the level of air pollution back then.

## **Real barriers to economic development in Los Angeles.**

In Los Angeles County, private automobile registration per capita was 0.539 in 1990. In 2012 it was 0.597, a gain of 11 percent. (Los Angeles Almanac 2014) By contrast, the pattern in San Francisco is different. It was lower in both years and it increased less there over that period. (Data Mart 2014) So the inference is that Los Angeles is more “car-friendly” than San Francisco. What is lost by an urban area being more car-friendly? Obvious costs are congestion and air pollution. Less obvious are the substantial hidden costs the city imposes on landlords, tenants, and landowners in general.

Most of the barriers to economic development identified in Los Angeles relate to zoning laws that restrict “land assembly,” and to off-street parking requirements for residences and offices. Those barriers are not perceived as such because they are indirect, but they do have profound adverse effects. Two goals of smart urban planning are infill development, and raising population density. Current zoning laws and parking requirements in Los Angeles block both.

### **Land Assembly Barriers**

Zoning laws typically permit developers to build large multi-family structures on large lots. But in a built-up urban area, gaining a large lot for development requires land assembly. Holdouts from land assembly for constructing multi-family buildings are a major barrier. Because of the obvious scale economies of larger sites, they are worth more per square foot. Owners of lots may hold out from land assembly, hoping to own the last parcel needed and therefore bargaining for a higher price.<sup>1</sup>

The most effective way to deter holdouts and enhance incentives for land assembly to small parcel owners is through graduated density. Higher density allowed on one acre or more gives developers economic incentive to buy contiguous lots. If base density is less than developers desire, the city could offer a significant density bonus for larger sites, i.e., graduated density zoning. Such steps provide an enticing incentive for assembling contiguous parcels (Shoup

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<sup>1</sup>A famous holdout is a small corner parcel in New York City at West 50th Street and 6th Avenue. There stands a modest three-story building dwarfed by the massive Rockefeller Center built in the 1930s. (Shoup, 2008)

2008). At present graduated density zoning is not on the books in Los Angeles.<sup>2</sup> With present high rents and chronic short supply of multi-family apartments in LA City and County, zoning changes that promote density could boost supply, slow rent increases, stimulate infill development, and boost improved land values. The result would be increased city and county property tax revenues.

### **Residential Off-Street Parking Requirements**

A multi-family structure in the City of Los Angeles must provide off-street parking amounting to an average of 2.25 parking spaces per dwelling unit. Residents do not pay directly for that off-street parking. It is included in rents and condo prices. As such, it is invisible and appears to many as “free parking.” And so when other parking is not “free,” users resent paying.

How costly is the “free” residential parking in Los Angeles? An unattended residential garage with 24/7 access requires 330 square feet of space per vehicle. That area, of course, includes the space devoted to aisles and maneuvering space. In a potential eight-unit building, effectively limited to seven units because of the off-street parking requirements, the required garage area would be 2,310 square feet (7 x 330). The estimated cost would be \$147,840 (2,310 x \$64 per square foot). That sum amounts to anywhere from 30 to 40 percent of the multi-family total construction cost, not a trivial amount (Shoup 2011). If tenants and owners could choose to buy or rent off-street parking, rather than have its price bundled into the dwelling unit’s rent or price as a take-it-or-leave-it deal, rents and condo prices could be lower.

A thorough statistical analysis of the effects of bundled residential parking (i.e., where the price of parking is included in the rent or purchase price of housing) shows that it boosts vehicle ownership. “(A)t the margin, hiding the cost of parking in the price of housing leads more people to own vehicles.” In addition, “reducing or eliminating minimum parking requirements

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<sup>2</sup>Another method for promoting land assembly by overcoming holdouts is through land assembly districts (LADS). “By forcing owners to reveal their reserve price, LADS promote efficient assemblies and deter inefficient ones. And by letting neighbors bargain for assembly gains, LADS can mitigate the unfairness surrounding condemnation.” (Heller and Hills, 2008)

– which will likely reduce the incidence of bundled parking – will also reduce vehicle ownership and by extension vehicle use.” (Manville 2014, p. 41)

Unnecessarily high housing costs in a metro area such as Los Angeles are barriers to economic development, and bundled residential parking in Los Angeles boosts the price of housing 30 to 40 percent, as shown above. “Los Angeles is now the most unaffordable housing market in the country... Los Angeles housing prices have grown about four-times faster than incomes since 2000.” (Ray, Ong, & Jimenez 2014, p. 2) These costs could be lowered in Los Angeles by unbundling the real cost of residential parking from the cost of housing.

Some tenants or owners faced with paying for parking might go from keeping two cars to one, or from one car to none. Shoup (1999) has noted that the cost of providing minimum parking is four times the cost of all other impact fees combined that cities generally impose. And further he notes, “Some cities allow a developer to pay a fee in lieu of providing the parking spaces required by zoning ordinances, and use this revenue to finance public parking spaces [in the neighborhood] to replace the private parking spaces the developer would have provided.” (Shoup 1999, p. 307)

Los Angeles should give developers the option of paying such a fee in lieu of providing required parking spaces.<sup>3</sup> The fee per space should be set significantly lower than the cost to a developer of providing the space. That margin of saving would induce paying the fee rather than providing the spaces. Public parking spaces built and operated by the city should not be free to users. The combined effect of in lieu fees and city provided fee (not free) parking is to reduce the supply of parking and the demand for parking, important achievements for economic development. A zero price always induces greater demand than a positive price. Free parking maximizes driving, imposing hidden costs of congestion and pollution as well as higher housing costs for renters and owners. Even better than in-lieu fees as an alternative to developers providing parking

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<sup>3</sup>In-lieu fees are discussed below.

would be to abolish residential off-street minimum parking requirements and to replace them with maximum allowed off-street parking instead of the current required minimum.<sup>4</sup>

### **Commercial Off-Street Parking Requirements**

The Los Angeles MSA is the third largest office market in the U.S., behind New York and Washington D.C. But less than 14 percent of the Los Angeles office stock is in the central business district, i.e., downtown. Thus, it ranks only 14<sup>th</sup> out of the 15 largest MSAs in the share of office space downtown. (Drennan & Brecher 2012) That ranking partly reflects path dependence in that Los Angeles is a post-automobile big city. Dallas-Fort Worth and Miami-Fort Lauderdale are post-auto cities as well, and their shares of downtown office space are similarly low, 15.5 and 12.9 percent respectively. But part of the explanation for LA's dispersion may be the onerous and costly parking requirements imposed by the City of Los Angeles on office buildings.

Zoning laws in Los Angeles require two parking spaces per 1,000 square feet of office space, adding substantially to construction costs. For example, a 100,000-square-foot office building must provide 200 parking spaces. So the 100,000-square-foot building must provide 66,000 square feet for parking (200 spaces x 330 square feet per space).

Using a recent construction cost estimate, the building cost - apart from the parking - is \$158 per square foot. The parking cost is \$108 per square foot for underground parking. Thus, the cost of the building alone is \$15.8 million (200,000 x \$158/square foot), and the cost of parking is \$7.1 million (66,000 x \$108). The total cost is \$22.9 million, and so required parking is 31 percent of the total. Above-ground parking would amount to about 24 percent of the total. (Shoup 2014, pp. 92 & 94). Even that percentage represents a substantial boost in office

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<sup>4</sup>Such a program has been imposed in London. For apartment buildings near public transit in London, the maximum allowed off-street parking is one space per dwelling unit. An analysis after the change of the effect on adding parking spaces showed that developers, left to their own judgment (limited only by the maximum allowed), produced only 52 percent of the parking spaces that would have been required under the old minimums. Shoup observed about that result, "...the previous minimum parking requirement almost doubled the number of parking spaces that developers would have voluntarily provided on their own." (Shoup 2014, p. 107)

construction cost compared with suburban areas that may have no, or less onerous, parking requirements.

### **In-Lieu Fees**

Some U.S. cities have in-lieu fees (mentioned earlier) to replace, in whole or in part, required parking. Such a fee should be lower than the true cost of a parking space in order to induce developers to opt for the fee rather than constructing the parking spaces. As a result, office construction costs would be substantially reduced, making the Los Angeles urban core more competitive with suburban locations. As with proposed residential in-lieu fees noted above, public spaces built and operated by the city with in-lieu revenues should not be free to users. The effect, as with residential in-lieu fees, would be a reduction in supply of parking and a reduction in demand for parking that is no longer “free.” That is, the cost would become visible to the user.

### **Building Conservation**

There are grand old office buildings in downtown Los Angeles that have not been renovated for modern office use because of the prohibitive cost of providing required parking at two spaces per 1,000 square feet. They have been renovated for residential use thanks to a city law passed in 1999, the Adaptive Reuse Ordinance (ARO). As Manville points out, “the neighborhood has the nation’s largest collection of intact office buildings built between 1900 and 1930 (many of them exemplars of West Coast Beaux Arts and Art Deco) and is listed on the National Register of Historic Places.” (Manville 2013, p. 53). The ARO exempted “old vacant commercial and industrial buildings in its downtown from all parking requirements if converted to residential use.” (Manville 2013, p. 49)

The ARO in Los Angeles has been a stunning success, boosting the supply of renovated housing units in downtown Los Angeles. In the 30 years from 1970 to 2000, housing growth in downtown was only about 4,000 units. But in the 10 years 2000-2010, 9,000 units were added and 6,000 of them were ARO units. “Downtown Los Angeles is only one case, but what

happened there lends support to existing arguments for ending residential minimum parking requirements.” (Manville 2013, p. 63)

In short, the ARO story is one of gentrification with positive results. Empty buildings are both dangerous and subject to rapid deterioration. Additionally, boosting downtown LA’s population with upper-income professional households probably cuts vehicle miles traveled by shrinking commuting distances.

### **Transit-Oriented Development**

Although Los Angeles has ambitious existing and planned subway and light-rail lines, there have been very few transit-oriented development (TOD) plans. Such plans would make the rail and overall transit system more financially viable if ridership were induced by economic incentives. Subways, light rails, and buses are alternatives to cars. If the City of Los Angeles made residential and office parking directly paid for by users at the same time transit use became more available and more frequent, there most likely would be a drop in car use and a rise in rail and bus use.

There are, or will be, six rail lines in Los Angeles. They generally will run along major thoroughfares. What is strongly needed is an overhaul of zoning and parking requirements along the transit corridors. Implementation of both graduated density and *maximum* off-street parking of one parking space per housing unit along those routes could greatly increase population density and ridership. In return for that cost reduction for developers (no required parking), the cost of the parking should be separated from the cost of the building so that condo prices and rents are net of parking.

Developers should be required to break out the price/rent of a parking space from the price/rent of a housing unit. The buyer/renter would then have the option to choose the housing unit alone or the housing unit and the parking space. Eliminating required parking spaces might induce developers to build more studio and one-bedroom units, housing that is in short supply.



Landlords would offer parking spaces on a monthly fee basis to residents. Tenants could choose to rent a parking space or not. Presumably, the nearby transit option as well as the lower rent or condo price would induce some tenants to forego the no-longer-free parking.

The experience of the ARO program downtown, described in the previous section, suggests that buyers/renters would choose less parking than the city presently mandates. Much of the current rail routes is lined with low-density, cluttered 1-2 story commercial development. Graduated density should allow five story buildings, greatly increasing the land value from current use, and thus providing a strong incentive for land assembly by owners of small lots.<sup>5</sup>

### **Failed Urban Economic Development Policies**

Local urban economic development must be focused upon a *place*. The place must be an appropriate spatial unit, that is, a labor market area. A neighborhood is too small, as is a census tract. Even a municipality is usually too small. A state – in contrast – is too big. But a metropolitan area is the right size because it forms a labor market.

The ultimate goal of local urban economic development is to raise per capita income and employment of residents of the metropolitan area. That objective requires directing efforts at *traded goods and services* industries. Such industries are those whose sales or revenues come in large part from *outside* the metropolitan area. A focus on mostly local non-traded industries such as retail trade and personal services is a mistake.

The most widely used strategy of local and state governments for increasing demand for labor is offering financial incentives to attract new establishments or retain existing establishments. The usual form of these incentives is a local tax abatement. But review in the development literature of financial incentives granted by state and local governments over the past decades reveals:

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<sup>5</sup>An example of transit oriented development stretching back to the early 20th century that remains viable today are the north-south avenues in Manhattan outside the central business district and along north-south subway lines. Those avenues are lined with 5 story attached buildings with commercial establishments on the ground floor and residential units on the four top floors. The appearance is uncluttered because of signage restrictions.

- a) There is a high cost per new job created.
- b) The resulting job expansion is unlikely to offset loss of tax revenue.
- c) If incentives are used, upfront incentives with claw-back provisions (penalties for non-performance or for moving away) are better than strung-out incentives with no penalties.
- d) Local governments rarely know if a financial incentive was really required to retain a threatened move-out. (Bartik 2009).

These financial incentives nationally amount to a massive transfer of scarce public dollars to the private sector, and they are generally not cost effective. One analysis of 129 local governments' use of financial incentives found that "economic growth is negatively associated with level of business incentive use." In addition, use of incentives "raise(s) concerns that in time of economic crisis, competitive pressure to use business incentives may trap local governments in a race to the bottom."<sup>6</sup> (Zheng and Warner 2010, p. 334

Unfortunately there are no national data on all financial incentives given by local governments annually to businesses. Because financial incentives in the form of tax abatements, the most popular type, are not local government expenditures but rather foregone tax revenues, they do not come under the scrutiny reserved for direct expenditures. Mayors like it that way, unless they are forced to disclose the costs.<sup>7</sup>

## **Film and TV Incentives**

The most noteworthy financial incentive affecting Los Angeles – and backed by California's governor – is the tax incentive for state film and television production. Originally about \$100

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<sup>6</sup>One sad example relates to a chronically depressed state – Michigan. An analysis of tax abatements by local governments in Michigan found that "few municipalities place conditions upon abatements, most never evaluate the performance of firms granted abatements, and abatement requests are seldom or never rejected... (C)osts appear to be significant although benefits, at best, (are) uncertain." (Sands et al 2006, p. 44)

<sup>7</sup>The only local governments required by state law to document the amount of annual tax expenditures in the form of tax abatements to business are the large municipalities of New York State. In 2013, the New York City foregone tax revenues in property tax exemptions and abatements awarded to business amounted to \$4.6 billion, or nine percent of the city's expenditures that year (City of New York 2013). Not a trivial amount.

million, it clearly was not working at keeping big productions in the Los Angeles area. In the summer of 2014, the governor proposed raising that to about \$300 million annually, and that step was approved beginning in fiscal year 2015-2016.

Hours of filming in Los Angeles have fallen drastically since the mid-1990s. The primary cause is competition from other states luring film production with more generous subsidies. In 2010, film studios won \$1.5 billion in financial commitments from state governments (Thierer 2012). But a meta-survey by the Center on Budget & Policy Priorities showed appalling returns (revenues gained per dollar of subsidy) for the states.

Excluding the questionable studies done by Ernst and Young for New York and New Mexico, all the other states included had revenue returns per dollar of subsidy ranging from \$0.07 to \$0.28. (Tannenwald 2010) In other words the film and TV financial incentives are big losers among so-called economic development programs. But it is similar to an irrational arms race. States will be tempted to offer more subsidies to lure more feature film production, and their actions will spur other states to do the same. In the end a massive amount of money has been transferred from the public to the private sector while the total production of films and TV shows remains the same.<sup>8</sup>

### **Enterprise Zones**

One form of financial incentive often used by local governments to increase demand for labor has been a costly and stunning failure across the nation. So-called “enterprise zones” aim at a “place” within a metropolitan area such as a neighborhood or census tract. Enterprise zones tend to shift existing employment to the designated enterprise zone from elsewhere in the metropolitan area. Therefore, they do not raise per capita income or employment in the metropolitan area, and so they contribute little or nothing to economic growth.

The enterprise zone is an economic development program aimed at moving jobs to poor neighborhoods, which has been shown to be far more expensive and far less successful than

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<sup>8</sup>The City and County of LA do not offer financial incentives to film and TV. But they have developed a program to encourage film and TV production by making it easier to obtain filming permits through an entity known as FilmLA.

moving poor people to jobs. One study showed enterprise zone jobs cost \$40,000 to \$60,000 each and many of the so-called created jobs were simply moved from non-covered areas. (Gramlich and Heflin 1998) A study of 75 enterprise zones over 13 states found few local decisions made in response to place-based tax incentives. That study failed to establish a significant positive effect of an enterprise zone upon employment. (Peters and Fisher 2002) Another large scale analysis of the effects of enterprise zones in two states (California and Florida) found “no evidence that these enterprise zones affected the employment of zone residents.” (Elvery 2009, p. 44)

Los Angeles’ experience with the enterprise zone strategy has been much the same as the sad results elsewhere. The Los Angeles Revitalization Zone (LARZ) program ran for the period 1992-1998, awarding place-based tax credits. Its advantage over similar programs was that it did not limit its aid to the very worst areas. A study of the effects of the LARZ program imposed careful controls over both the number of building permits issued and their value in LARZ zones compared with the rest of Los Angeles. The authors concluded that “even under moderate economic conditions (not the worst areas), such programs can be relatively ineffective.” (Spencer & Ong 2004, p. 380) Similarly, the State of California – after a period of promoting enterprise zones – realized that the zones were ineffective; there were better uses for the foregone taxes. The State Enterprise Zone (SEZ) program was shut down at the end of 2013.

### **Metropolitan Area Growth is the Key**

What has been found to improve the employment rate and reduce the poverty rate in central *cities* is an expanding *metropolitan* economy. A careful econometric analysis of 269 metropolitan areas and their central cities for 1995 showed that metropolitan employment growth in the previous seven years had a significant negative effect upon central city poverty. Also, the level of per capita personal income in the larger metropolitan area had a significant negative effect upon central *city* poverty. (Drennan 2002)

Those results contradict the assumption that underlies the enterprise zone development policy, namely that the urban poor are in “a ghetto in which race or ethnicity is combined with class in

a spatially concentrated area whose residents are excluded from the economic life of the surrounding society” (Marcuse & van Kempen 2000, p. 19) That is, the jobs must be brought to them because they are “excluded from the economic life of the surrounding society.” Apparently they are not excluded. The city’s poor *do* gain from general metropolitan economic growth.

## **Conclusion**

The depressing lesson of the previous section is that state and local governments are not skilled at promoting local economic development. Their favored policies, financial incentives in the form of tax abatements or credits, are less-than cost effective. Indeed, they collectively amount to a massive transfer of scarce public resources to the private sector.

In light of that sad lesson, what can the City of Los Angeles do to promote urban economic development? It can do three things. The first is central to urban economic success: mind the store. That is, tend to mundane matters very well (public safety, transportation, trash collection, primary and secondary education). The second is to remove barriers to local economic development. And the third is to avoid wasting money on dubious tax incentives.

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**Table 1: Employment in Los Angeles MSA, All Industries, Grouped by Losers, Winners, and Cyclical: 2001, 2007, and 2011**

Industry Groups	Employment in Millions			Change: 2001-2007	Change: 2007-2011	Average Wage
	2001	2007	2011			
Losers	2.0	1.7	1.5	-12.4%	-10.3%	\$80,073
Winners	1.4	1.6	1.7	14.4%	6.7%	\$44,719
Cyclical	4.0	4.5	4.1	12.0%	-7.7%	\$57,013
<b>Total Employment</b>	7.4	7.8	7.4	5.9%	-5.4%	

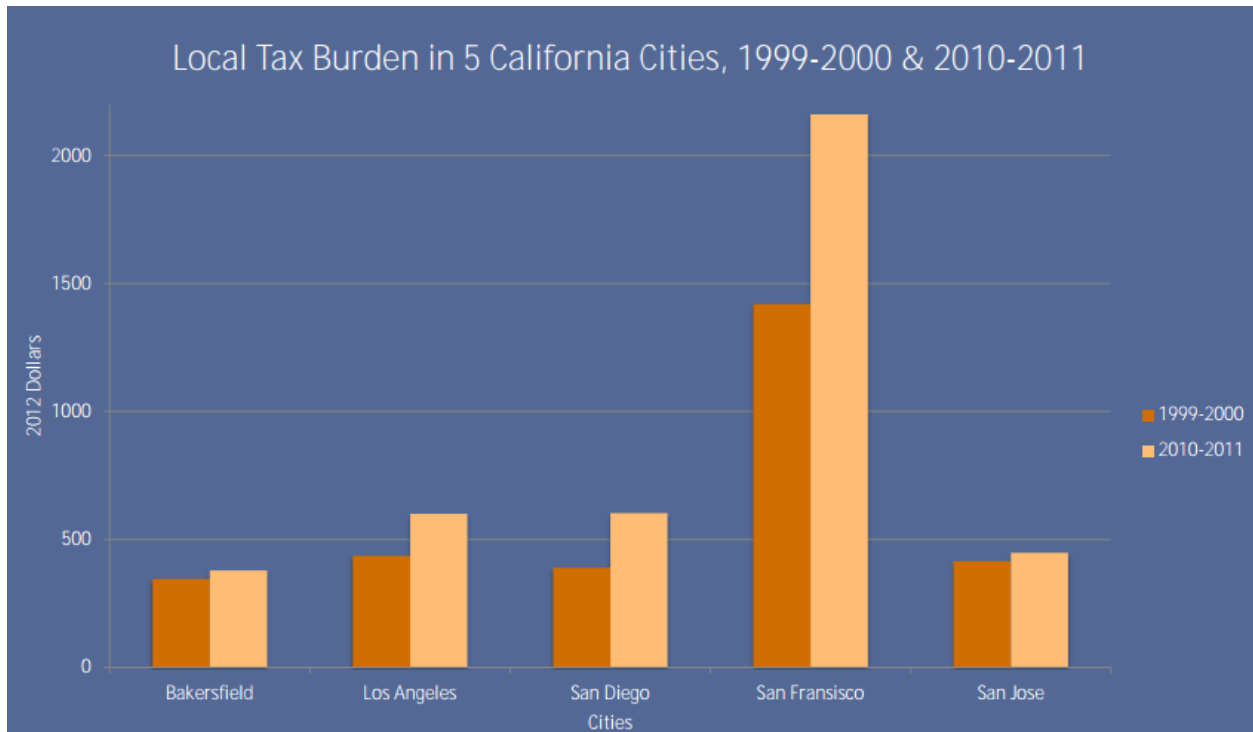
Details need not sum to totals due to rounding.

Note: *Losers* are eight industries with employment declines in 2001-2007 and 2007-2011.

*Winners* are five industries with employment increases in 2001-2007 and 2007-2011. *Cyclical* industries are those with employment increases in 2001-2007 and declines in 2007-2011.

Source: UCLA Luskin School of Public Affairs, *A View of the Region* (2013), available at <http://luskin.ucla.edu/sites/default/files/laulcommonground.pdf>

**Figure 1**



Source: UCLA Luskin School of Public Affairs, *A View of the Region* (2013), available at <http://luskin.ucla.edu/sites/default/files/laulcommonground.pdf>



# **CHAPTER 6**

## **Regulations for the Online Short-Term Rental Market in Los Angeles**

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There has been a boom in what has been termed the “sharing economy.”<sup>1</sup> This business model often taps into millennials’ increased need for flexibility as well as a generational shift from ownership to access.<sup>2</sup> Sharing companies thrive on their decreased reliance on human capital and infrastructure; they make use of underutilized resources and innovative technologies in order to lower transaction costs.<sup>3</sup> Often considered “disruptors” of older businesses, these companies strategically challenge the status quo for their own and their users’ benefits. Their business “disruptions” sometimes also involve the violation or evasion of existing legal statutes and ordinances deemed negligible, inapplicable, inefficient, or outdated. Cities and municipalities throughout the United States have struggled with how to best address these challenges.

Central to this new wave of peer-to-peer marketing platforms are short-term rental (STR) websites such as Airbnb, VRBO, and HomeAway. Building upon predecessors such as eBay and Craigslist, online STR platforms similarly facilitate transactions in a rapidly expanding market: individuals willing to rent part or all of their homes and travelers in need of short-term housing. Through these STR platforms, “operators” or “hosts” can advertise spaces ranging from a living room couch to large multi-room estates. Travelers have additional rental options at different price points beyond what is available from traditional hotels and motels. In exchange for this service, some STR platforms such as Airbnb charge both hosts and travelers fees for each interaction.

Airbnb’s dominance both in terms of market share and brand recognition has led to its being set as a standard for the STR industry overall. This rapid growth and dominance, however, has caused contention. The large market share held by Airbnb places the company at the center of much of the regulatory debate.

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<sup>1</sup>This chapter is based on an Advanced Policy Project (APP) for the degree of Master of Public Policy at the UCLA Luskin School of Public Affairs.

<sup>2</sup>Vincent Trivett, “What the Sharing Economy Means to the Future of Travel.” (2013), <http://skift.com/wp-content/uploads/2014/07/skift-what-the-sharing-economy-means-to-the-future-of-travel.pdf>.

<sup>3</sup>Darcy Allen and Chris Berg, “The Sharing Economy: How Over-Regulation Could Destroy an Economic Revolution,” (2014), [http://ipa.org.au/portal/uploads/Sharing\\_Economy\\_Media\\_Release\\_December\\_2014.pdf](http://ipa.org.au/portal/uploads/Sharing_Economy_Media_Release_December_2014.pdf).

## Regulatory Issues Facing Los Angeles and Other Local Governments

Proponents and opponents of STR platforms diverge in assessing their cost and benefits. Short-term rental proponents state that companies such as Airbnb provide a means for middle-class tenants to supplement their incomes as well as broaden their networks through short-term rentals.<sup>4</sup> Free market advocates assert that STR platforms such as Airbnb remove market inefficiencies.<sup>5</sup> In addition, STR platforms enable the use of underutilized living spaces that would otherwise be wasted resources.

Due to cheaper prices, Airbnb travelers seem typically to stay longer in their destination city than hotel guests, leading to an argument that STR platforms increase economic activity and generate more tax revenue for the host city.<sup>6</sup>

Conversely, opponents to short-term rentals argue that STRs and hotels operate on uneven playing fields. In addition to evading health and safety regulations enforced on hotels, the vast majority of STRs do not remit the Transient Occupancy Tax (TOT) remitted by hotels. In cities with a sizable tourism industry, this tax provides a substantial revenue stream. However, most online hosts do not comply since STR platforms such as Airbnb allow hosts to hide their names and addresses and continue to operate without fear of identification.

These factors incentivize the commercial operation of STRs in traditionally residential neighborhoods. Opponents charge that owners and renters now list rooms for tourists as opposed to procuring more long-term tenants and roommates, stripping permanent rental housing units from an already scarce rental market. The loss in Los Angeles is said to be

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<sup>4</sup>Los Angeles Short Term Rental Alliance, "Testimonials," accessed February 1, 2016, <http://www.la-stra.org/testimonials/>; Fraiberger, Samuel P., Sundararajan, Arun, Peer-to-Peer Rental Markets in the Sharing Economy, 1-14, (2015), [http://www.hbs.edu/faculty/conferences/2016-dids/Documents/Fraigerber\\_Sundararajan\\_March2016.pdf](http://www.hbs.edu/faculty/conferences/2016-dids/Documents/Fraigerber_Sundararajan_March2016.pdf); Tomio Geron, "Airbnb Had \$56 Million Impact On San Francisco: Study." *Forbes* (2012), <http://www.forbes.com/sites/tomiogeron/2012/11/09/study-airbnb-had-56-million-impact-on-san-francisco/>.

<sup>5</sup>Benjamin G. and Geradin and Edelman Damien, "Efficiencies and Regulatory Shortcuts: How Should We Regulate Companies like Airbnb and Uber?" (2015), 1-32. <http://hbswk.hbs.edu/item/efficiencies-and-regulatory-shortcuts-how-should-we-regulate-companies-like-airbnb-and-uber>.

<sup>6</sup>Vincent Trivett, "What the Sharing Economy Means to the Future of Travel." *Skift* (2013), <http://skift.com/wp-content/uploads/2014/07/skift-what-the-sharing-economy-means-to-the-future-of-travel.pdf>; Airbnb, "New Study: Airbnb Generated \$632 Million in Economic Activity in New York - Airbnb," accessed March 15, 2016, <https://www.airbnb.com/press/news/new-study-airbnb-generated-632-million-in-economic-activity-in-new-york>; Tomio Geron, "Airbnb Had \$56 Million Impact On San Francisco: Study." (2012), <http://www.forbes.com/sites/tomiogeron/2012/11/09/study-airbnb-had-56-million-impact-on-san-francisco/>.

between 1,000 and 7,200 such units.<sup>7</sup> Furthermore, they argue that STR platforms “alter neighborhood character,” create additional traffic and parking shortage, and lead to increased safety hazards.<sup>8</sup>

Current debates in Los Angeles mirror those taking place in other cities. Within the City of Los Angeles, both Mayor Eric Garcetti and City Council are now engaged in discussions and rule-making processes. These efforts began in March 2014 when a memo by Allan Bell, Deputy Director of City Planning, sought to address the general uncertainty about the status of residential STRs offered through online platforms. The memo indicated that such operations are in fact banned for the majority of units in residential zones, and that others are required to register as a business with the city and to pay the TOT.<sup>9</sup>

In early 2015, Councilmember Mike Bonin met with community members on both sides of the issue, from STR hosts and disgruntled residents to advocacy groups. By June 2015, Wesson and Bonin put forth a motion providing guidelines for the Department of City Planning to follow in crafting STR regulations. And in May 2016, the Los Angeles Department of City Planning provided the City Planning Commission with a set of recommended regulations.<sup>10</sup>

Following a period of public hearings, the Planning Commission backed the proposals with a few amendments, making the regulations eligible for a vote by City Council.<sup>11</sup> At this writing, a voting session is yet to be scheduled in Council. However, alongside these regulatory efforts, other Los Angeles officials have engaged in discussions with Airbnb. In July 2016, they finally

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<sup>7</sup> Airbnb, “Report: Housing & The Airbnb Community in the City of Los Angeles,” 2015; Roy Samaan, “Airbnb, Rising Rent, and the Housing Crisis in Los Angeles.” (2015), <http://www.laane.org/wp-content/uploads/2015/03/AirBnB-Final.pdf>.

<sup>8</sup> Fred Brousseau, “Policy Analysis Report: San Francisco,” (2016), <http://sfbos.org/sites/default/files/FileCenter/Documents/55575-BLA.ShortTermRentals%20040716.pdf>; Matt Stevens and Martha Groves, “Malibu to Crack down on Short-Term Rentals via Airbnb, Other Websites,” *Los Angeles Times*, May 27, 2014. Accessed March 15, 2016, <http://www.latimes.com/local/la-me-malibu-renting-20140528-story.html>.

<sup>9</sup> Alan Bell, “Short Term Rentals FAQ - Memo,” (2014), [http://cityplanning.lacity.org/code\\_studies/misc/shorttermrentals.pdf](http://cityplanning.lacity.org/code_studies/misc/shorttermrentals.pdf).

<sup>10</sup> Los Angeles Department of City Planning, “Recommendation Report,” (2016), <http://planning.lacity.org/ordinances/docs/HomeSharing/StaffRept.pdf>.

<sup>11</sup> Emily Alpert Reyes, “L.A. takes step toward new rules on short-term rentals,” *Los Angeles Times*, June 23, 2016, <http://www.latimes.com/local/lanow/la-me-ln-airbnb-rentals-20160623-snap-story.html>.



signed a deal whereby the company agreed to collect and to remit the TOT to the City on behalf of its hosts.<sup>12</sup>

The proposed regulations include the following main components:

- The definition of true home-sharing is limited to using one's own primary residence (defined as the location where the host resides for at least 6 months of the year).
- Home-sharers are required to register through the Department of City Planning *and* to pay the TOT and obtain a certificate from the Office of Finance.
- Renters of units under the Rent Stabilization Ordinance (RSO) cannot engage in home-sharing.
- Permits are non-transferrable and must be renewed every two years.
- Advertisements of STRs are required to display permit numbers.
- Platforms are required to remove illegal listings.
- Platforms are required to disclose data to the City on a monthly basis.
- Violating platforms and hosts are fined, ranging from \$200 to \$2,000 per day.
- Application fees are to be determined at a later date.

## **LA's Regulatory Background for STRs**

In what follows, we first present a numerical *analysis* of the Airbnb market in Los Angeles. Then we discuss the most common problem faced by other cities while attempting to regulate this market: *enforcement* difficulties. Finally, we provide an analysis and recommendations for several key components of the proposed regulations in light of the enforcement challenges and available enforcement pathways.

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<sup>12</sup>Emily Alpert Reyes, "Airbnb strikes deal with L.A. to collect millions in lodging taxes," *Los Angeles Times*, July 18, 2016, <http://www.latimes.com/local/lanow/la-me-ln-airbnb-taxes-20160718-snap-story.html>.

## Analysis of the Airbnb Market in Los Angeles

To put the proposed regulations and enforceability issues into context, it is essential to understand the scope of the local Airbnb market. Since the inception of online platforms, the STR market has grown significantly in Los Angeles. Founded in 2008, Airbnb now controls an estimated 64.6% of the market in Los Angeles.<sup>13</sup>

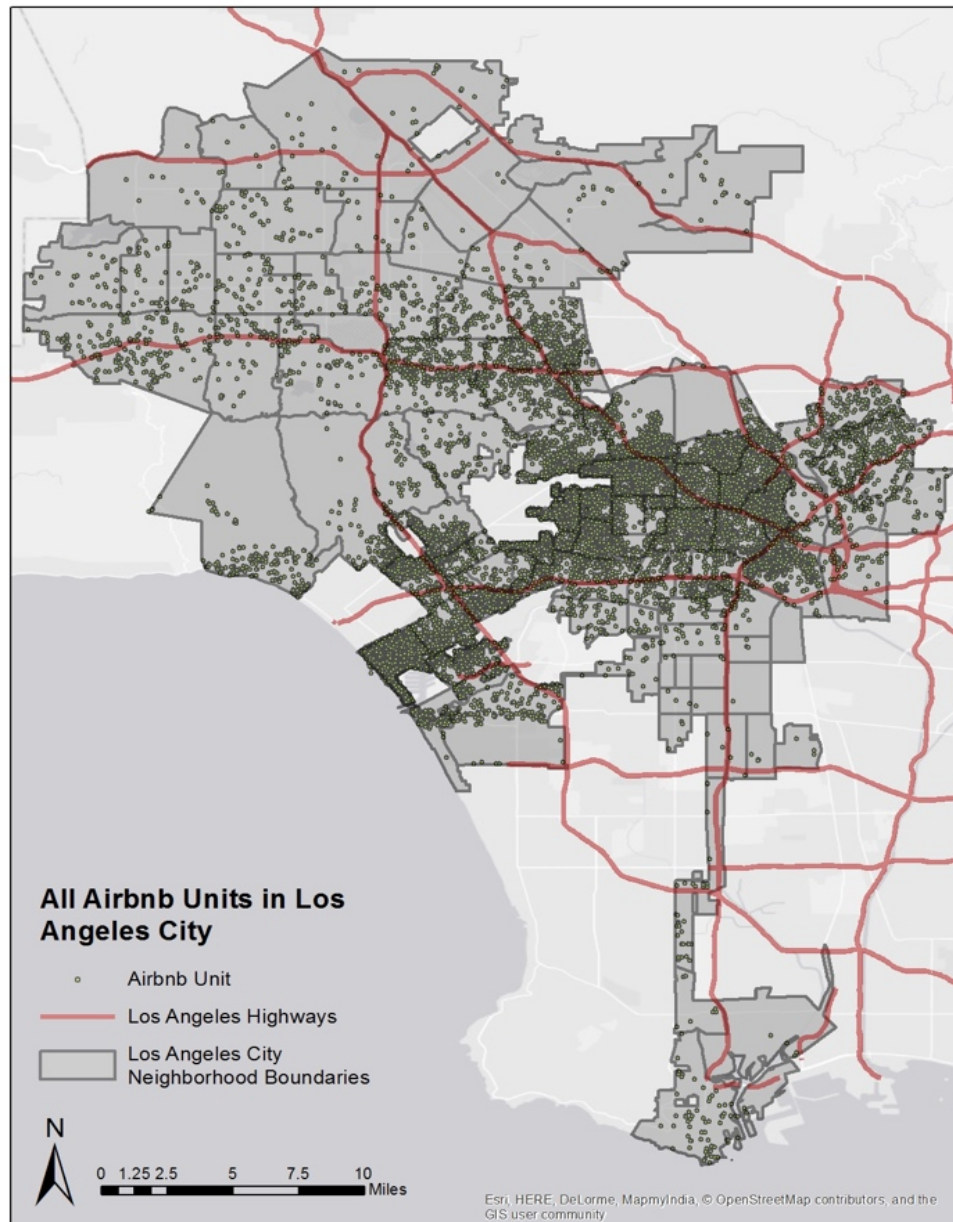
**LISTINGS.** Our analysis found that in 2015, there were 21,675 active Airbnb listings (i.e., at least one day booked) across the City of Los Angeles (Figure 1) and 31,709 across all of Los Angeles County. Of those active in the City of Los Angeles in 2015, nearly 64% (13,954) were entire homes or apartments, 31% (6,707) were private rooms and only 5% (1,014) were shared rooms.

**HOSTS.** These listings were offered by 14,708 hosts in Los Angeles. 20% of all hosts had more than one listing while 119 hosts had more than 10 listings and one had 59 listings. It is important to note that while the majority of hosts did not have more than one listing, these findings are limited in that, from the data available, it is impossible to discern whether the units' are the hosts' primary residence or not. A share of these listings are likely the secondary residence of such hosts. Additionally, hosts with more than one listing may not be listing individual units but rather individual rooms in one unit. However, even with these consideration, the reported numbers point to the prominence of the Airbnb market in Los Angeles.

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<sup>13</sup>Roy Samaan, "Airbnb, Rising Rent, and the Housing Crisis in Los Angeles" (2015), <http://www.laane.org/wp-content/uploads/2015/03/AirBnB-Final.pdf>.

**Figure 1. All Airbnb Listings in the City of Los Angeles in 2015**



Airbnb's report on STRs in Los Angeles indicated that 82% of hosts conducted home-sharing of their primary residence. From data accessible by the public (and by extension to government officials), it is impossible to arrive at exact numbers since listings do not indicate whether the unit is the host's primary residence. Using various algorithms, our analysis shows that at least 11% of hosts (1,676) are operating commercially or are minimally operating two unique

units/properties. These 11% are responsible for 30% (6,240) of the Airbnb listings, a sizable portion of the market.

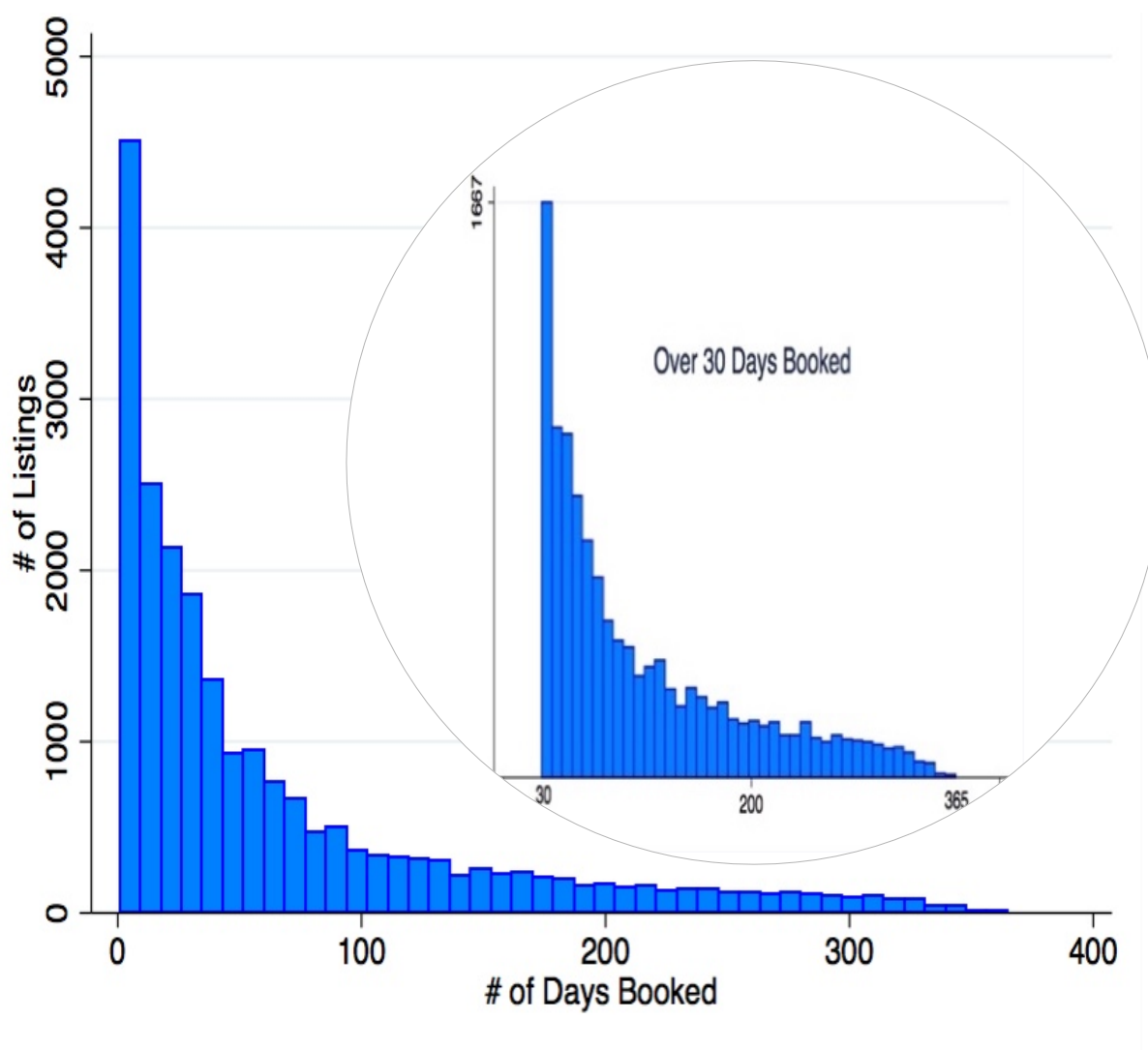
**Table 1. Breakdown of Number of Days Booked by Listing**

Days Booked in 2015	Number of Units	Percent of Units
1-14 Days	6,150	28.37%
15-30 Days	3,979	18.36%
30-60 Days	4,086	18.85%
60-90 Days	2,172	10.02%
90-364	5,286	24.39%
365 days	2	1%
<b>Total</b>	<b>21,675</b>	<b>100%</b>

**BOOKINGS.** Half of all units were rented out for less than 34 days but over a third of all units were rented out for more than 2 months (60 days) out of the year. On average, each listing was booked for nearly 66 days (Standard Deviation [SD] = 77) out of the year. This number, however, differed widely between hosts.

As previously mentioned, over 20% of hosts had more than one listing. These hosts, on average, had rented out all of their multiple listed units for 204 days out of the year (SD = 363, median = 92). This total is in stark contrast to hosts with only one listing with 53 days booked out of the year (SD = 64, median = 29). These numbers reflect the potential effect of the Airbnb market on long-term housing.

**Figure 2. Distribution of Number of Days Booked in 2015**



**PRICES.** Across Los Angeles, entire homes or apartments were booked for an average of \$213.41 per night (SD = \$252.33, range = \$10 - \$5,299), private rooms were rented out for \$80.84 on average (SD = \$59.28, range = \$11 - 1823.00), and shared rooms were booked for an average of \$47.12 per night (SD = \$25.66, range = \$10 - 342.5).

## Analysis of Enforceability Problems

Currently, the illegal proliferation of short-term rentals stems from lack of effective enforcement pathways available through the Los Angeles Municipal Code (LAMC). Any motion passed by City Council will be futile without effective enforcement. Nearly every major city in the United States (such as Portland, New York and San Francisco) that has attempted to regulate the STR market has encountered the same enforcement obstacles. In comparing STR registration numbers to total number of Airbnb listings after passing of regulations, we note low levels of compliance: Portland 7-8%, Austin 20%, Grand Rapids 5.7%, Chicago 2.7%, and San Francisco 5.7%.<sup>14</sup>

Current conversations in Los Angeles City Hall have somewhat centered on ensuring enforceability of the proposed motion.<sup>15</sup> Based on our analysis, enforcement difficulties in Los Angeles can be attributed to three factors: 1) The large pool of violators, 2) Difficulty in identifying violating units, and 3) Legal hurdles for penalizing a violator once identified.

**LARGE POOL OF VIOLATORS.** Beyond blatant disregard for the laws, the large pool of violations stems from lack of awareness of STR laws. In residential zones that do allow for STRs, many STR operators often do not understand their status as a business and the consequential requirement of registration, acquisition of permits or tax payments.<sup>16</sup> In addition to registering as a business, the Los Angeles Municipal Code also requires that those operating transient occupancy units also display their “Transient Occupancy Registration Certificate” conspicuously

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<sup>14</sup>Steve Law, “Airbnb Resists City Efforts to Regulate It,” *Oregon Local News*, accessed February 1, 2016, <http://portlandtribune.com/pt/9-news/244479-112102-airbnb-resists-city-efforts-to-regulate-it->; Marielle Mondon, “Austin Pilot Program Looks at Realities of Enforcing Short-Term Rental Laws,” *Next City*, July 17, 2015, <https://nextcity.org/daily/entry/city-council-may-crack-down-on-short-term-rentals>; Josh Sidorowicz, “Airbnb Licensing to Pick up Speed in GR, City Manager Promises Enforcement,” *Fox17*, November 14, 2014, <http://fox17online.com/2014/11/13/airbnb-licensing-to-pick-up-speed-in-gr-city-manager-promises-enforcement/>; Danny Ecker, “Here’s How Big Airbnb Has Gotten in Chicago,” *Crain’s Chicago Business*, n.d.; Dale Carlson, interview by Kiana Taheri and Blake Valenta, January 5, 2016.

<sup>15</sup>Tricia Keane, interview by Kiana Taheri and Blake Valenta, December 21, 2015; Matt Glesne, interview by Brian Nguyen, Kiana Taheri and Blake Valenta, November 24, 2015.

<sup>16</sup>Lauren Herstik, “Did You Just Get a \$500 Freelance Assignment? The City Might Bill You \$30,000,” *L.A. Weekly*, September 2015. <http://www.laweekly.com/news/did-you-just-get-a-500-freelance-assignment-the-city-might-bill-you-30-000-6040715>.

on the premises.<sup>17</sup> Even if a host is aware of these requirements, however, under the current ban of residential STRs, hosts would be unable to comply through business registration.

**IDENTIFYING VIOLATORS.** The City also currently has no effective means of identifying those in residential units who are violating their respective zoning by conducting STRs or enforcing the ban.<sup>18</sup> Compliance is left up to the integrity of each resident. STR platforms such as Airbnb post ads show pictures of the property and coordinates on a map. However, the map coordinates are often rough estimates and can be off by several blocks. Pictures are often of the interior of the unit which hinders external identification even if one were physically to arrive at the rough map coordinates. Furthermore, many listed units are within apartment buildings which complicates identifying the exact violating unit.

**PENALIZING VIOLATORS.** Additionally, even if identified, the City currently has no effective means of penalizing violators. The primary mechanism for identifying violators has been through complaints submitted to the City by neighbors. The City then submits a cease and desist notice. Our interview with Los Angeles City staff in charge of processing complaints indicated that if a violator does not respond properly to the cease or desist notice, then the case is commonly forwarded to the Office of the City Attorney.<sup>19</sup>

However, at this time, no follow up has been made on any of these cases as the city lacks sufficient evidence to prosecute violators. Online advertisements of STR platforms or even accounts by neighbors of STRs do not suffice. Instead, the City Attorney requires evidence of a transaction *and* actual short-term occupancy by a renter in order to process these cases. To have this evidence, then, the monitoring department would have to book a room and spend the night to acquire sufficient evidence. Since penalties are unlikely, many individual hosts have no incentive to register.

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<sup>17</sup>American Legal Publishing - Online Library, "Chapter II, Licenses, Permits, Business Regulation," accessed February 1, 2016, <http://library.amlegal.com/>.

<sup>18</sup>Tricia Keane, interview by Kiana Taheri and Blake Valenta, December 21, 2015.

<sup>19</sup>Jeff Paxton, interview by Brian Nguyen, Kiana Taheri, and Blake Valenta, December 23, 2015.

## Analysis of Proposed Regulations

We now turn to analysis of three core components of the proposed regulation: 1) Data disclosure by STR platforms, 2) Requirement for displaying permit number and removal of illegal listings, and 3) Fee amount of the application process. All three would be needed for a complete regime of regulatory enforcement.

*DATA DISCLOSURE.* Data disclosure requires STR platforms to turn over their user and booking data regularly to government agencies. A proposed Los Angeles ordinance would demand the following information:

- Home Sharing registration number,
- Address of all sites maintained, authorized, facilitated or advertised by the Hosting Platform for Transient use during the period,
- Total number of nights that the residential unit was occupied during the period and
- Amount paid for each stay.<sup>20</sup>

These data could then be cross-checked by City code enforcement officers with extant registration systems for the purpose of verifying compliance. Many observers claim that having a database of hosts and units simplifies and eases the process of enforcement.<sup>21</sup> Without specific information such as host name and address, identification of listings in violation of the law is time consuming and of limited effectiveness. With identifying data, it can be a relatively straightforward procedure to match hosts' identifying data from the STR platform with the City's STR registration data. However, research into the literature around disclosure and analysis of current efforts in Portland calls into question the ability of data disclosure by itself to aid enforcement.

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<sup>20</sup>STR Ordinance Draft – CPC-2016-12435-CA

<sup>21</sup>Steve Law, "Airbnb Resists City Efforts to Regulate It," *op. cit.*



**COMPANIES ARE ADEPT AT EVASION OF DISCLOSURE LAWS.** Even though the process of cross-checking would be straightforward, it would not be simple or cheap. There is substantial literature analyzing how companies have grown skilled at skirting disclosure requirements; they adhere to the letter of the law in such a way as to make the data they disclose useless for the original purpose intended.<sup>22</sup> STR platforms would most likely provide raw un-aggregated data. Disaggregated data contain the building blocks of the four data fields outlined in the ordinance. However, someone must put assemble them in a way that is meaningful for enforcement purposes.

Disaggregated data would leave the City no choice but either to develop systems to read the data or, alternatively, devote city analyst hours to process the data – a costly venture. The City may choose to pursue the development of a software that automatically matches the business registration number on the STR platform database with the database of registered businesses.<sup>23</sup> While technically feasible the City does not possess the software development skill set needed, requiring costly outside development. This process would have to be redone if the STR platform alters the manner in which it provides the data. It would also need to be done separately for each STR platform currently operating and any others that arise in the future. Due to these complications, more likely, the City will have the equivalent of code enforcement officers in charge of manually cross-checking the databases. This method will incur high operating costs in terms of staff time.

**MAJOR STR PLATFORMS WILL LITIGATE THE ISSUE.** Technology companies such as Airbnb view user data as primarily a privacy issue and are fiercely protective.<sup>24</sup> They are likely to contest demands to turn over the data all the way to the Supreme Court. Evidence of this reluctance is present in Portland and from our interviews with STR platforms.<sup>25</sup> In January 2015, Portland revised its ordinance to require “booking agents” to turn over name and addresses of hosts to the Revenue Bureau to ensure compliance with remittance of TOT.<sup>26</sup> However, despite the

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<sup>22</sup> Fung, Archon, Mary Graham, and David N. Weil. 2007. *Full disclosure: the perils and promise of transparency*. Cambridge. Cambridge University Press.

<sup>23</sup> J.R. DeShazo, Interview by Brian Nguyen, Kiana Taheri, and Blake Valenta, December 16, 2015.

<sup>24</sup> Paavo Monkkonen, interview by Brian Nguyen and Blake Valenta, December 1, 2015.

<sup>25</sup> David Owen, interview by Brian Nguyen, Kiana Taheri, and Blake Valenta, January 20, 2016.

<sup>26</sup> Ibid.

ordinance being in place, Airbnb, HomeAway, and other STR platforms have refused releasing of user data.<sup>27</sup>

Legal experts are skeptical of the STRs' ultimate chance for success arguing that "if you have a showdown with a government, you are probably going to lose... When push comes to shove, the government will get the data it wants."<sup>28</sup> However, much political pushback exists toward requiring STR platforms to provide data to government. A common critique is the notion of government overreach with regard to private individual data in order to search for and identify law-breaking.

There are some legal precedents for the proposition that some government demands for disclosure are unconstitutional, for example *City of Los Angeles v. Patel*.<sup>29</sup> The U.S. Supreme Court ruled in that case that police do not have a right to examine the registries of hotels without a search warrant. In the Portland lawsuit, there is a chance that the court might rule that the ordinance overreaches. At a minimum, the almost certain cycle of lawsuits and appeals will result in a long period in which enforcement is encumbered by a lack of identifying data. The threat of lawsuits further complicates the political feasibility of this policy options as the City is unlikely to have an appetite for lengthy court cases stemming from any regulations passed.

**REQUIREMENT FOR DISPLAYING PERMIT ID.** Requiring STR listings to display a permit number allows cities to distinguish between legal and illegal STRs. In order to obtain and display a permit number, STRs must first register with the City and meet the legal requirements of the ordinance. Since the burden for compliance is placed on the platform, a display of permit number acts as a signaling mechanism for the city. An enforcement agent that can easily identify whether STR platforms are in compliance by the number of listings that lack registration numbers.

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<sup>27</sup> Steve Law, "Portland to Crack down on Airbnb Hosts Who Fail to Get Permits," *Portland Tribune*, January 21, 2015. <http://portlandtribune.com/pt/9-news/247793-116145-portland-to-crack-down-on-airbnb-hosts-who-fail-to-get-permits->

<sup>28</sup> David Reiss, Interview by Brian Nguyen, Kiana Taheri, and Blake Valenta, December 20, 2015.

<sup>29</sup> Supreme Court of the United States, "*City of Los Angeles, California v. Patel et al*," 2015. <https://supreme.justia.com/cases/federal/us/576/13-1175/>.

One of the most important questions facing Los Angeles officials is how to distinguish “good” and “bad” rentals.<sup>30</sup> This regulation directly addresses that hurdle. For this mechanism to be effective, active cooperation is required from STR platforms. However, STR platforms may resist such agreements as this verification process may result in the loss of too many STR listings. By levying large fines against STR platforms for illegal listings, the incentive to only have registered STR advertisements shifts from hosts to STR platforms. STR platforms would then need to police their own listings, therefore pressuring hosts to register as a business and remove unregistered listings or face legal and financial repercussions.<sup>31</sup> This approach would sever the unregistered STR hosts from easy access to customers, strangling their business until they comply with the law.

Other cities have already instituted similar measures. Cities such as Portland, San Francisco, Anaheim, and Santa Monica have put the onus of the display of STR registration numbers in ads on STR platforms in addition to STR operators. In early 2015, Portland passed an ordinance that prohibited STR platforms from displaying advertisements without permit numbers.<sup>32</sup> Similarly, in 2016, San Francisco passed an ordinance requiring STR platforms to ensure all listings were in compliance with registration number posting requirements.

STR platforms have taken up different avenues of resistance in response. In Portland, HomeAway has refused to comply with the ordinance. As a result, in late 2015, Portland proceeded with a lawsuit against HomeAway. That case is still pending at this writing. More recently, Airbnb has gone on the offensive preemptively suing cities, such as San Francisco, Anaheim, and Santa Monica, which have passed such laws.<sup>33</sup> STR platforms, such as Airbnb, claim that governments cannot hold online STR platforms accountable for the behavior of their

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<sup>30</sup>Emily Reyes, “L.A. officials want to keep Airbnb-type rentals from being ‘rogue hotels’,” August 25, 2015, *Los Angeles Times*. <http://www.latimes.com/local/lanow/la-me-ln-airbnb-rental-regulations-20150825-story.html>.

<sup>31</sup>Jon Bell, “Portland Seeks \$2.5M in Lawsuit over Short-Term Rentals,” *Portland Business Journal*, accessed February 2, 2016, <http://www.bizjournals.com/portland/blog/real-estate-daily/2015/10/portland-seeks-2-5m-as-city-clamps-down-on-short.html>.

<sup>32</sup>Steve Law, “City, Short-Term Rental Hosts Face off,” *Oregon Local News*, accessed February 29, 2016, <http://portlandtribune.com/pt/9-news/248329-116358-city-short-term-rental-hosts-face-off>.

<sup>33</sup>Kendall, Marisa, “Airbnb fights unfriendly regulations with wave of lawsuits against San Francisco, other cities,” *Mercury News*, September 18, 2016. <http://www.mercurynews.com/2016/09/18/airbnb-fights-unfriendly-regulations-wave-lawsuits-san-francisco/>.

users – that is, cities cannot force STR platforms to demand that their users display permit numbers in their advertisements.<sup>34</sup>

The outcomes of these lawsuits are as now unknown. What is known that Airbnb is refusing to back down and is committed to fighting this through the fullest extent of the legal process. Los Angeles must be prepared to wage a long and potentially protracted legal battle.

**APPLICATION PROCESSING FEE.** At this writing, the cost of the home-sharing application process has yet to be determined in the proposed regulations.<sup>35</sup> While recognizing the possibly uncommon nature of this recommendation, we highly recommend that the applications be free for all users. Mandatory fees provide an additional barrier to registration, especially for operators who earn little income from STRs. For the STR operators that only rent out a couch for a few days a year, even a small permitting fee would impede on their ability and/or willingness to register. By removing these barriers, STR operators have no excuse to not acquire a permit.

A free application process would also supplement the requirement to display permit numbers in ads. Simplifying the permitting process would maximize the number of legal STRs with permit numbers on STR platforms. By maximizing permit applications of legal STR operations, the City can more effectively identify and prosecute illegal operations. Thus, a free and streamlined process is an essential key to more effective enforcement. After establishing a free registration process, the City of Santa Monica now has about a 50% STR registration compliance rate – a rate much higher than all reported compliance rates from other cities.<sup>36</sup> A higher number of registered hosts means a higher amount of TOT revenue for the City, a portion of which can be put towards the administrative cost of processing the applications.

## Future Directions & Opportunities

Los Angeles' proposed ordinance contains many reasonable attempts to grapple with the perplexing issue of STR enforcement. All proposals are being enacted through the

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<sup>34</sup>David Owen, interview by Brian Nguyen, Kiana Taheri, Blake Valenta, January 29, 2016.

<sup>35</sup>Los Angeles Department of City Planning, "Recommendation Report," 2016.

<http://planning.lacity.org/ordinances/docs/HomeSharing/StaffRept.pdf>.

<sup>36</sup>Salvador Valles, interview by Kiana Taheri and Blake Valenta, December 23, 2015.

administrative code and may ultimately rely on legal avenues for compliance. However, increased compliance can be achieved outside a legal framework. To minimize barriers to hosts' compliance with the City's STR regulations and to facilitate enforcement, the City should seek special agreements with STR platforms.

Regulations, while a crucial part of the process, are restricted to what the City can legally compel an STR platform to do. Good policy need not rely solely on legal mandates. It can instead involve mutually beneficial agreements outside of the regulatory process. Independent agreements also have the advantage of demonstrating the commitment of the City to supporting innovation and technological advances. STR platforms benefit from these agreements as these agreements legitimize their business models and can facilitate successful Initial Public Offerings (IPOs) of stock.

The City has already secured one such agreement with Airbnb in which, instead of hosts individually calculating and remitting the 14% Transit Occupancy Tax owed, Airbnb adds the TOT fee to a STR renter's transaction.<sup>37</sup> Airbnb then annually remits to the City the TOT collected throughout the year. Another agreement the City should explore with all STR platforms is incorporating the permitting application in the STR platforms' online host signup process.

We recommend the City pursue agreements with large STR platforms to incorporate an option for hosts to comply with the City's permitting process. This option could be in form of a checkbox by which hosts can authorize the STR platform to collect and send host information to the Department of City Planning for permit processing. The box would warn that, in the City of Los Angeles, a STR host must have a valid permit number to operate and failure to post this valid permit number could lead to sanctions. Thus, the host's operational and mental hurdles to complying would be minimized.

With a system needed to receive the permit data from the STR platform, there would be a certain backend cost to the City for such a process. There may also be increased costs from a

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<sup>37</sup>Airbnb, "How Does Occupancy Tax Collection and Remittance by Airbnb Work? | Airbnb Help Center," n.d.

back and forth process as the City collects and verifies all the requisite information needed to confirm STR regulation compliance. However, the money is well spent assuming the City gains a much higher permit application rate. In addition, this option ensures that those hosts choosing not to check the box and obtain permits have been given fair warning which increase the chance that prosecution of violators will be perceived as fair by the public.

For the STR platform, the option would provide another opportunity to reduce the administrative burden of its users and position the complying STR platforms as leaders in sharing economy/city partnerships. The key factor to making the recommendation palatable to STR platforms is that those who do chose not to check the box do not have their information forwarded to the City's STR permitting department. Those whose information is sent to the City have opted for this service. Since hosts using the box have agreed to have their data forwarded to the City, they can be no perception of STR platforms having improperly provided host data to the City.

### **Data-Driven Enforcement Strategy and Penalties**

In case of violation, the proposed regulations places fines on both the platforms and the hosts ranging from \$200 to \$2,000 per violation. Designating high dollar amounts for fines is a common practice by government agencies, stemming from the belief that increasing the average cost of violation will deter such behavior. However, research shows that a “low-violation equilibrium”—where the majority of actors adhere to the law — occurs in situations where potential violators perceive a high *probability* of being penalized, rather than simply a high cost in case of penalization.<sup>38</sup>

For cities dealing with the online STR market, this approach translates into investing in potentially high cost efforts to identify names and addresses of offending hosts. In the short-run, such enforcement activities will produce the perception of a high probability of penalization. This perception will then dissuade those considering violating the regulations, eventually reducing illegal STR activity throughout the city. In the long-run, a significantly lower

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<sup>38</sup>Mark Kleiman and Beau Kilmer. “The Dynamics of Deterrence.” *Proceedings of the National Academy of Sciences of the United States of America*. Vol. 106, no. 23 (2009): 14230–35. doi:10.1073/pnas.0905513106.

amount of the TOT revenue will need to be put towards enforcement. Los Angeles should follow this strategy.

The City would need to invest in adequate enforcement capacity to achieve the perception of high probability. Thus, we recommend that the revenue generated through the TOT agreements be allocated towards active enforcement. To achieve optimal results, the City should pursue a data-driven strategy for online monitoring while also dedicating code enforcement officers to respond to neighborhood complaints.

**DATA DRIVEN STRATEGY.** The City should focus enforcement efforts in areas where 1) the public perceives the problem to be most acute, and 2) there is a high chance of encountering an egregious violator. By harnessing Airbnb listing data from 2015, we have constructed a heat map shown on Figure 2 that assesses LA regions by enforcement priority. The heat map highlights regions with high concentrations of commercial Airbnb listings and rent stabilized units. In this way a code enforcement officer can initially prioritize their online monitoring on select areas of the City rather than all active Airbnb listings.

**MONITORING.** As previously discussed, by requiring hosts to post permit numbers in ads, the City greatly lowers the administrative costs of determining which of the posted ads are complying with the law. Monitoring should be done as a combination of online monitoring of the STR platform's website and in-person inspections. We identified at least three cities where active monitoring was taken up as an enforcement mechanism: Austin,<sup>39</sup> Santa Monica,<sup>40</sup> and Paris.<sup>41</sup>

**NEIGHBORHOOD COMPLAINTS.** We recommend that the City also utilize neighborhood complaints as another mechanism for identifying violators. There are two advantages to the complaint process. First, it helps identify the most egregious violators. Complainants are commonly very willing to provide addresses of violators and help the City match online advertisements with actual units.<sup>42</sup> This assistance reduces the identification cost for the City enforcement officers. Second, a functioning complaint system

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<sup>39</sup>Farzad Mashhood, "As Austin short-term rental rules take effect, hundreds breaking them during ACL Fest weekend," *Statesman*, October 10, 2012. <http://www.statesman.com/news/news/local/as-austin-short-term-rental-rules-take-effect-hund/nSZbj/>.

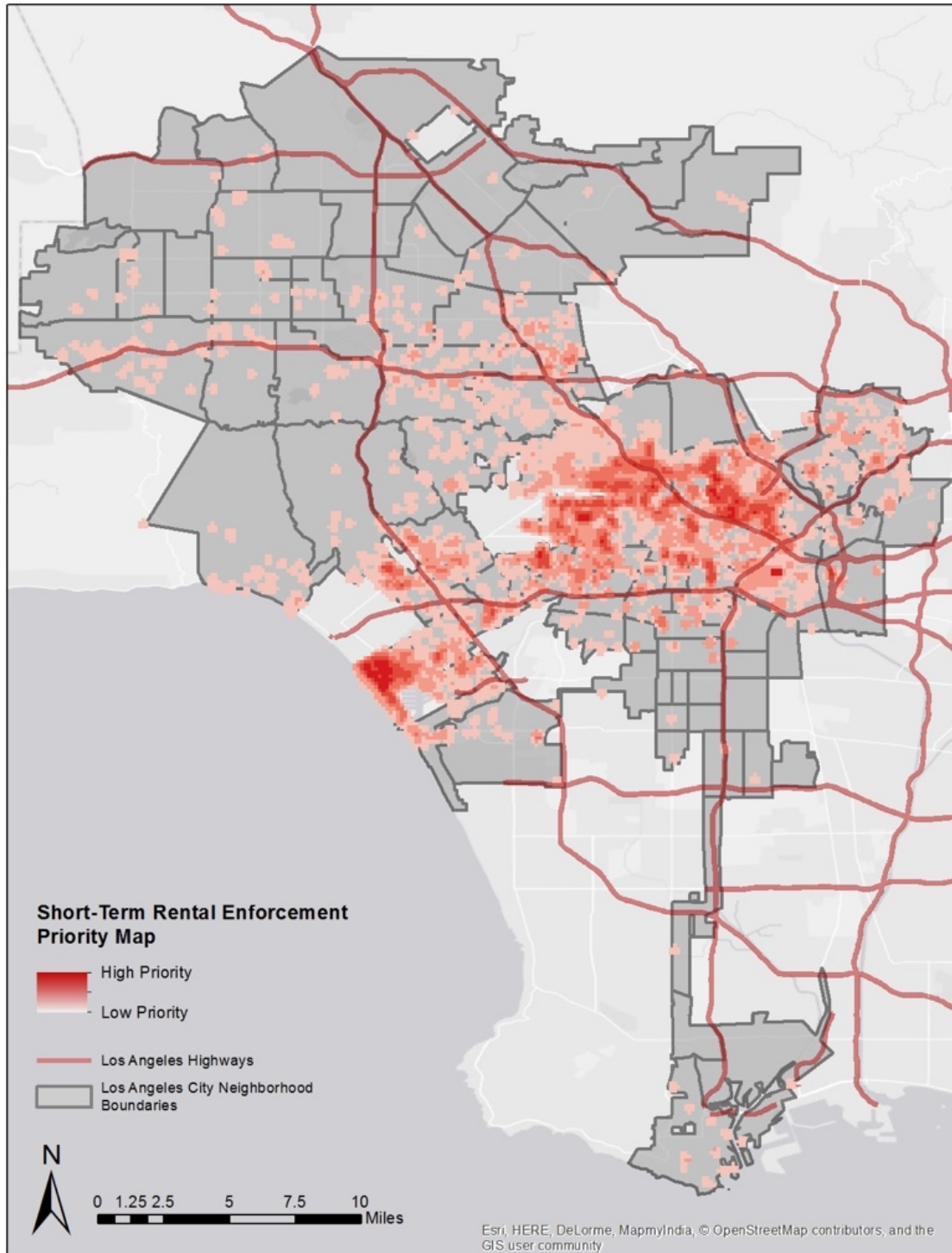
<sup>40</sup>Planning & Community Development - City of Santa Monica, "Short-Term Rental Home-Share Ordinance"; Salvador Valles, interview by Kiana Taheri and Blake Valenta, December 23, 2015.

<sup>41</sup>Helene Fouquet and Ania Nussbaum, "Paris Cracks down on Airbnb Rentals, Raids Apartments," *Seattle Times*, August 14, 2014. <http://www.seattletimes.com/life/travel/paris-cracks-down-on-airbnb-rentals-raids-apartments/>.

<sup>42</sup>Salvador Valles, interview by Kiana Taheri and Blake Valenta, December 23, 2015.

is necessary to create an aura of surveillance from one's neighbors. The risk of being turned in increases the perceived probability of being sanctioned for not obtaining a permit.

**Figure 2. Short-Term Rental Enforcement Priority Map**





## **Conclusions**

The City of Los Angeles can learn from the experiences of other cities. It is well known that STRs will resist regulation by municipal authorities, if they can. But accords can be reached with them that make it less likely that costly litigation will ensue and more likely that compliance will occur. A combination of data disclosure on hosts by the STRs and then enforcement using those data will be needed. Hosts using the STRs need to have a sense that the probability of being caught evading local regulation and taxation is high. Arrangements can be reached with STRs for hosts to register voluntarily according to local requirements. Appropriate taxes can be collected by the STRs and remitted to City authorities. Once the necessary data are obtained from the STRs, they can be used for targeted enforcement along with complaint mechanisms open to neighbors who may be adversely affected by improper rentals. The City should invest sufficiently in enforcement in the initial period to give hosts a sense that compliance is important and that evasion will be detected.

# **CHAPTER 7**

## **The Affordable Care Act 2.0: Reimagining Health Care Reform in California**

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The Patient Protection and Affordable Care Act (PPACA, ACA, or “Obamacare”) was signed by President Barack Obama in 2010.<sup>1</sup> It represented the most significant health care reform since the establishment of Medicaid and Medicare in 1965. As a part of the ACA, many states created health insurance exchanges from which citizens can purchase qualified health plans (QHPs) with or without federal subsidies. Covered California (Covered CA) was the first of these state-based exchanges to be established, and has enrolled over two million Californians since its inception. In addition, almost three million Californians have been routed into its expanded Medi-Cal program.<sup>2</sup>

As of January 1, 2017, however, the health care landscape in California may change even further. At that time, individual states may apply for the 1332 State Innovation Waiver component of the ACA. This waiver, if approved, would allow a given state to modify its implementation of the ACA. States will be able to tailor health care reform to their state’s unique needs and preferences, while maintaining the basic protections and benefits of the ACA. This chapter suggests how Covered CA can best take advantage of the 1332 State Innovation Waiver to advance health care reform in California.

To explore this opportunity, we employed a data collection strategy of literature reviews, expert interviews, and data set analysis to understand the current health landscape of California. Based on our results, we sought the most recurring and viable themes, and we ultimately recommend three options:

- (1) Inclusion of undocumented adults under health insurance coverage;*
- (2) Increasing the shared responsibility payment (tax penalty) for non-coverage; and*
- (3) Creating a new qualified health plan for young adults.<sup>3</sup>*

We assessed each policy option based on our main criteria: goals (improving affordability and enrollment) and feasibility (political and fiscal).

## The 1332 State Innovation Waiver

Beginning January 1, 2017, states may apply for a component of ACA legislation termed the Section 1332 State Innovation Waiver. This waiver permits states to modify elements of the ACA in exchange for alternative state health care legislation. The intent of the waiver is to allow states to *pursue creative health reform strategies while retaining the basic provisions of the ACA*. State policymakers can use the waiver to advance a health care reform agenda that improves access to quality, affordable health insurance while allowing a state to account for its distinct needs and environment.

The 1332 Waiver allows states to create alternatives to the following ACA provisions:

1. The individual mandate to carry health coverage
2. The employer mandate to offer coverage
3. The premium and cost-sharing subsidies available in the exchange
4. The health benefit exchanges and essential health benefits requirement

However, there are fundamental provisions of the ACA that states cannot waive. These include the “stand-alone” components such as guaranteed issue, annual and lifetime coverage limitations, increased coverage of preventative care, and the requirement to allow dependents up to the age of 26 to be enrolled into their parent/guardians insurance plan.

Furthermore, any proposed reform must also follow four guiding principles regarding expected outcomes. Essentially these guardrails stipulate that any reforms must *improve* upon the ACA, not weaken its achievements. These four guardrails are:

1. Maintenance of the current level of coverage/enrollment
2. Maintenance of the current level of affordability
3. Maintenance of the current level of comprehensiveness of benefits
4. Maintenance of deficit neutrality (no added cost to the federal government)

Based on these guardrails, the ACA serves as a standard that states can attempt to improve upon via 1332 Waiver reforms. The guardrails ensure that any attempted reforms cannot detract from the ACA's core achievements. States will have to work closely with the federal Department of Health and Human Services (HHS) to demonstrate guardrail compliance.

In order to apply for the 1332 Waiver, states are required to pass authorizing legislation that details the reforms suggested to HHS and the Department of Treasury. In addition, states are required to provide a 10-year budget plan with supporting actuarial analyses. HHS reviews the health provisions, while the Department of Treasury reviews the budget plan with fiscal analyses. The waiver can be approved for up to five years and can be renewed. Lastly, the 1332 Waiver also includes an option to submit a joint application with the analogous 1115 Medicaid/Medicare Waiver to pursue more comprehensive reforms.

This chapter will address the following policy question: How best can Covered CA take advantage of the 1332 waiver to advance health care reform in California? The chapter covers only the three options we ultimately endorse. Our full analysis, including the analysis of the rejected options, appears in the original report provided to Covered CA.

### **Recommendation: Inclusion of Undocumented Adults in Health Coverage Expansion**

California's undocumented immigrants represent 2.7 million of the nation's estimated 11 million.<sup>4</sup> Within California, the undocumented make up 6% of the overall population and 41% of the uninsured population, an estimated 1.4-1.5 million.<sup>5</sup> It is important to remember that these individuals are often part of families with mixed documentation status. Indeed, 40% of adult undocumented immigrants live with U.S.-born children. An estimated 13% of California's school children have at least one undocumented parent.<sup>6</sup>

Although the ACA has made remarkable achievements in expanding affordable health coverage to California's uninsured population, the estimated 1.4 to 1.5 million undocumented immigrants have been left out of these improvements due to eligibility requirements under ACA that include citizenship status. Thus, undocumented immigrants in California are not

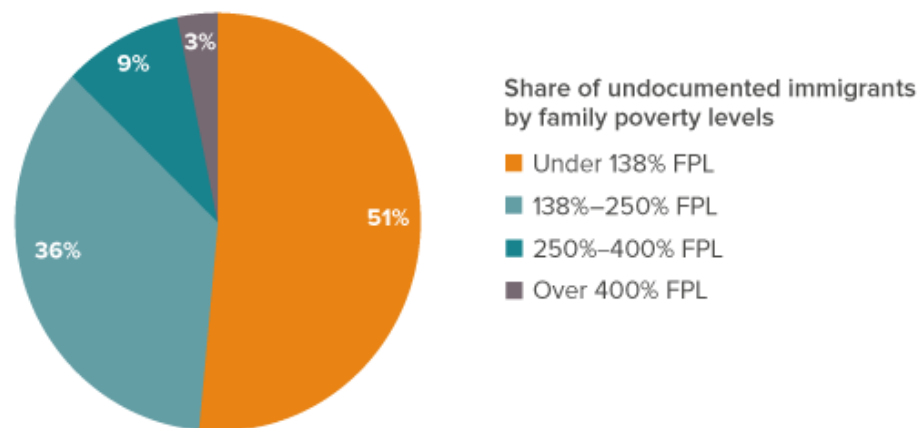
eligible to purchase Covered CA health plans, *with or without cost assistance*. As a result of such limited access, it is not surprising that undocumented individuals are 27% less likely to have visited a doctor in the previous year.<sup>7</sup> Because of this infrequent access to care, undocumented immigrants with chronic and infectious health conditions are more likely to present at later stages of the disease.<sup>8</sup> Thus, undocumented immigrants may experience more serious and costly health repercussions due to limited access to quality health care.<sup>9</sup>

### **Increased Coverage**

Many observers view the current uninsured rates among the undocumented population as a problem that desperately needs to be addressed. The 1332 Waiver was intended to help states tweak the ACA to serve their unique needs and populations better. Thus, offering coverage to undocumented individuals is the type of challenge that could be tackled in the next iteration of California's health care reform.

The key to predicting enrollment effects is to examine the income distribution within this population. As depicted on Figure 1, roughly half of the undocumented population have incomes in the Medi-Cal range and the other half have incomes in the Covered CA range. Only 3% have incomes over 400% of the Federal Poverty Level (FPL), the upper limit of the ACA's cost assistance provisions. Due to this income distribution, even if undocumented immigrants were allowed to enroll in Covered CA plans, most individuals would not be able to afford its private plans.

**Figure 1: Income Distribution of Undocumented Individuals**



SOURCE: Authors' calculations using IRS tax data from the [Brookings Institution](#), population data from the [American Community Survey](#), and statewide undocumented population estimates from the [Center for Migration Studies](#). Data from 2013.

Source: McConville S, Hill L, Ugo I, Hayes J. Health Coverage and Care for Undocumented Immigrants. PPIC. November 2015. [http://www.ppic.org/content/pubs/report/R\\_1115SMR.pdf](http://www.ppic.org/content/pubs/report/R_1115SMR.pdf)

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Most undocumented individuals between ages 18-29 report health outcomes similar to documented young adults. By examining the take-up projections for documented adults of this age category, we gain insight on the likelihood of undocumented young adults taking up insurance.<sup>10</sup> Current estimates project that without the financial assistance of Advance Premium Tax Credits (APTCs) or Cost Sharing Reduction Subsidies (CSRs), the base take-up rate for young adults (ages 19-29) is about 58% or 340,000 individuals in 2017. For those between 251-400% FPL, the base take-up rate for the non-elderly documented individuals that are ineligible for subsidies is 55% or 580,000.<sup>11</sup>

Extending eligibility may allow some undocumented individuals to obtain health insurance through the exchange. However, affordability of plan premiums still remains a key issue for this group. As shown on Table 1, the monthly premium for an individual making \$2,000 per month can be up to \$331.



**Table 1: Premium Estimates for Single Adult and Family of 4**

			Contra Costa	Monterey	Orange	San Joaquin
Single adult, 25 years old, monthly income of \$2,000/mo	Bronze	Monthly premium % income	\$218 10.9	\$231 11.6	\$164 8.2	\$176 8.8
	Silver	Monthly premium % income	\$284 14.2	\$331 16.6	\$231 11.6	\$252 12.6
Family of 4, 2 adults (age 35), 2 children, monthly income of \$4000/mo	Bronze	Monthly premium % income	\$544 13.6	\$575 14.4	\$412 10.3	\$441 11.0
	Silver	Monthly premium % income	\$703 17.6	\$819 20.5	\$575 14.4	\$626 15.7

SOURCES: Covered California website, 2016 Shop and Compare Tool.

NOTES: Monthly premium costs are for the lowest priced plan available. For the family of 4, \$13 is added to the monthly premium cost to enroll children in Medi-Cal program.

Source: McConville S, Hill L, Ugo I, Hayes J. Health Coverage and Care for Undocumented Immigrants. Public Policy Institute of California. November 2015.

[http://www.pplic.org/content/pubs/report/R\\_1115SMR.pdf](http://www.pplic.org/content/pubs/report/R_1115SMR.pdf)

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For a family of four making \$4,000 a month, even the cheapest Covered CA plans have premiums of up to \$819. The Massachusetts Institute of Technology (MIT) living wage calculator tool indicates that individuals with a \$25,000 annual income should be paying approximately 8.74% of their income toward all medical expenditures, including premiums, copayments, and deductibles.<sup>12</sup> Yet, all but one of the premiums listed above surpass the mark for the suggested medical expenditure. Thus, without financial assistance, many undocumented families are likely to find health insurance unaffordable even if they are able to participate in the exchange.<sup>13</sup>

Another factor to consider is the possibility of risk pool change due to the inclusion of undocumented immigrants, which may alter current insurance premiums. Research has shown that undocumented immigrants are typically healthier than U.S.-born citizens.<sup>14</sup> For that reason, extending eligibility to this group may aid in mitigating risk for offered insurance

plans.<sup>15</sup> Therefore, enrolling the undocumented population may decrease overall premium prices and benefit *all* enrollees through increased affordability.

### **Political Feasibility**

There are many indications pointing to a favorable political climate for expanding coverage to undocumented adults. In late 2015, California extended eligibility for full-scope Medi-Cal coverage to undocumented children through Senate Bill (SB) 4, approved by a 28-11 vote.<sup>16</sup> With this new law, approximately 170,000 of California's children became eligible for health coverage beginning May 2016.<sup>17</sup> Although this legislation still left over a million undocumented adults without insurance, its passage indicates a supportive political climate for such measures in the legislature.

Moreover, SB10 was introduced into the state Senate. It proposed California's application for the 1332 waiver in order to allow for undocumented individuals to obtain coverage through Covered CA. It is clearly evident that California's governing body is aware of the gap in coverage available to undocumented immigrants, and has already made significant steps to address it. SB10 was signed by Governor Brown in June 2016. It now remains for the state to pursue obtaining the waiver. The political uncertainty at this writing is at the federal level, i.e., the outcome of the presidential election and, thus, the fate of the ACA.

### **Fiscal Implications**

Allowing undocumented individuals to access Covered CA plans will not impose costs to the federal or state governments. Instead there may be potential long-term cost savings for health care if these individuals' take-up, as they may now access preventative care. Allowing the undocumented population to purchase into the state's exchange removes a legal barrier. It does not, however, expand subsidy eligibility to undocumented individuals. But if both eligibility *and* cost assistance measures were made accessible to undocumented immigrants, this would significantly reduce the uninsured rates in this population.

For the documented population, the base take-up rate in 2017 for young adults is projected to be 63% with subsidies. By federal poverty level, the base take-up rates with subsidies are projected to be 70% (139-200%), 60% (201-250%), and 53% (251-400%).<sup>18</sup> Given these increasing take-up rates with subsidies, the undocumented population is likely to have similar take-up patterns. To comply with the “deficit neutral” guardrail of the 1332 Waiver, allocation of state funds would be needed to offer cost assistance to undocumented individuals and families between the 139-400% FPL. This step would cost an estimated \$1.3 billion.<sup>19</sup>

In short, if the state wants to treat undocumented individuals and all others equally, it would need to add significantly to its expenditures on health care. While support might be found in the legislature for such spending, Governor Brown might well oppose it for reasons of fiscal prudence. What his successor might do after the 2018 gubernatorial election is unknown.

### **Recommendation: Increase the Shared Responsibility Payment**

By increasing enrollment and requiring both healthy and unhealthy individuals to purchase health insurance in the same risk pool, an individual mandate removes adverse selection from the marketplace. Adverse selection absent a mandate will occur because healthy individuals are less likely to purchase insurance than individuals with health problems. The larger and healthier risk pool that emerges with a mandate thus translates to greater affordability for consumers since the average cost per covered individual is lowered. Under ACA, uncovered individuals are not strictly mandated to buy coverage, but they pay a tax penalty (shared responsibility payment) if they don’t. Thus, the individual mandate tax penalty is a mechanism by which the ACA achieves affordability *en masse*, by incentivizing the uninsured individuals to take up health insurance.

Despite the major increase in health insurance uptake since the ACA was enacted, there still remain 2.8 million Californians without insurance. Surprisingly, many Americans are still not aware of the penalty, making it ineffective as a motivating agent. A 2015 Urban Institute survey found that approximately 4 in 10 uninsured adult Americans are unaware of the tax penalty.<sup>20</sup>

In California, the knowledge of the penalty was above the national average. Approximately 18% of respondents were not aware of a tax penalty.<sup>21</sup>

Available research regarding optimal tax penalties may aid in California's decision-making. Massachusetts had a health insurance plan that served as a model for the national ACA. Economists have analyzed Massachusetts' early ACA-like reform data to determine an optimal penalty amount. They concluded that the minimum tax penalty that implements universal coverage levels would be 24.9% of the premium or \$1,462 per year.<sup>22</sup>

Thus, raising the tax penalty to something approaching \$1,462 could achieve greater enrollment while still remaining within a reasonable scope of affordability. To help the individual mandate achieve what it intended to achieve, a moderate increase to the tax penalties may better incentivize the uninsured to purchase health insurance. If the state imposed its own tax penalty of 2.5% of an individual's income, and if all of the uninsured continued to remain uninsured, we estimate that the tax would bring in about \$1.25 billion in added revenue. Of course, many uninsured persons would respond by purchasing insurance. If *all* of them bought coverage, no revenue would be collected, so actual revenue would be less than \$1.25 billion but more than zero since the actual result would be between the two extremes.

On its surface, increasing the tax penalty seems like it would diminish affordability for the individual consumer. However, if a larger tax penalty increased enrollment, this change would further increase Covered CA's risk pool (i.e., it would reduce adverse selection) and ultimately yield lower premiums. Still, there is a trade-off. For those persons who ignored the penalty and remained uninsured, there would be an increased cost with no gain in personal coverage.

### **Enrollment Effects**

Overall, the existing individual mandate/tax penalty aided in increasing enrollment; without it, nearly 12.5 million individuals would have remain uninsured nationally.<sup>23</sup> Within California, by 2019, the individual mandate penalty at its current level is estimated to reduce the number of

uninsured persons by about a million (down to between 2 and 3 million).<sup>24</sup> By altering the penalties to provide a near equal financial trade-off (between being uninsured and paying the penalty and having insurance), California would further increase enrollment. Those persons eligible for insurance but remaining uninsured typically have incomes too high to qualify for Medicaid (Medi-Cal) or to obtain federal subsidies. Of course, it is important to consider that there are differed behavioral responses based on how an individual perceives a penalty, his/her price elasticity of demand, and the level of awareness of option in the health insurance market.<sup>25</sup>

### **Political Feasibility**

One of the major challenges the ACA faces in California is the general unfavorable view of the individual mandate.<sup>26</sup> Additionally, at least 41% of the American public are unaware of the tax penalty's existence.<sup>27</sup> If a higher penalty is implemented, families may face an unforeseen state *and* federal tax fine for not having health insurance in the upcoming years. In turn, this surprise penalty may cause resentment and even dissuade some families and individuals from purchasing health insurance.<sup>28</sup> As with most proposed tax increases, an increase in a tax penalty would likely be socially unfavorable. However, if efforts could be made to educate the public about good intentions of the increase, more public support could be obtained. Overall, applying a fixed *percentage* penalty within the state would be more progressive (less regressive) than a flat dollar penalty.

### **Fiscal Impact**

While higher penalties may produce some revenue, such revenue may be negligible if our main goal is to incentivize the uninsured to enroll in health plans. For the federal government, this policy option is fiscally feasible: the main costs to the federal government are an increase in federal subsidies for the newly insured, if they are eligible. This cost will be incurred regardless of a 1332 Innovation Waiver application because the uninsured population is projected to decrease over the years. According to the California Simulation of Insurance Markets (CalSIM) model, the uninsured will decrease from 2.20 million in 2016 to 1.89 million in 2019, or 310,000

newly insured individuals. Applying the average subsidy of \$303 for California, this new population, if eligible for subsidies, will cost the federal government about \$112 million per year starting in 2019.<sup>29</sup> That federal cost would be incurred as more Californians bought insurance thanks to the state penalty and thus became eligible for a federal subsidy.

As noted above, the imposition of a state penalty would raise some state revenue.

Massachusetts is an example. Tax penalties were used in that state as a mechanism to enforce the individual mandate. Massachusetts' policy was to penalize individuals based on income and age for up to half the cost of the lowest insurance premium available in the state health marketplace.<sup>30</sup> In 2012, a 27 year old individual earning above 300% FPL incurred a tax penalty of \$1,260 per year for opting out of buying insurance. The introduction of the mandate increased health coverage in Massachusetts by 19.4% and the state had additional revenue of \$94 million per year. In addition, there was an improvement in self-reported health status. As such, the individual mandate helped limit adverse selection and keep premium costs at an affordable level.<sup>31</sup>

### **Creating a New Qualified Health Plan for Young Adults**

Before the ACA's implementation, California's young adults (YA) between ages 19-34 were the demographic with the lowest rate of insurance: 67%.<sup>32</sup> By 2014, YA's rate of insurance coverage improved to 78.5%.<sup>33</sup> However, YA were still the least likely to be insured, particularly as compared to those over 64 (98%) and those under 19 (94%).<sup>34</sup> Despite such improvements, one in five young adults remain uninsured.<sup>35</sup>

Traditionally, health economists have attributed this high uninsured rate to YA perception of "invincibility".<sup>36</sup> Contrary to this belief, the majority of uninsured YA report that health insurance is a necessity (74%) and worth the costs (61%).<sup>37</sup> Moreover, 75% of YA reporting their health status as "excellent," YA indicated that health insurance is "worth the money" *more often* than some older age groups.<sup>38</sup> Nonetheless, there is a category of YA who apparently are willing to take the risk of going without insurance, perhaps gambling that they won't become seriously ill or injured.

Currently, the only ACA plan geared specifically toward YA is the Catastrophic Plan. It is only available to individuals under 30 years of age, and is designed to protect individuals from worst case scenarios.<sup>39</sup> The Catastrophic Plan has lower monthly premiums, but the highest deductibles. Co-pays are capped at \$35 or 50% co-insurance (whichever is lower) for the first one to three visits. One key downside of the Catastrophic Plan is that federal subsidies are not applicable.

Despite YAs' ostensible desire for health insurance, they are not purchasing the subsidized plans available for their income range. YA do have low health risks; over half (55%) of uninsured YA would save money by foregoing coverage in 2016 because their health costs plus penalties are below the cost of insurance.<sup>40</sup> But note that those odds are not particularly good, especially when possible catastrophic risks are considered.

Research on pre-ACA YA (18-25) health utilization has shown that uninsured YA spent an average of \$1,040 (\$1,150 in 2016 dollars) in out-of-pocket health care costs.<sup>41</sup> This amount is considerably less expensive than having the most basic coverage for a YA in California. As an illustrative example, for a 27 year old with an annual income of \$30,000, a bronze plan with 1-2 doctor visits costs \$1,900 to \$2,300 annually.<sup>42</sup> Even after adding the tax penalty of \$750 to the out-of-pocket costs of \$1,150, the total is still less than paying for insurance by hundreds of dollars. For YA without any health expenditures, foregoing coverage is even more appealing.

Young adults clearly value health insurance, but may find themselves struggling with affordability despite the availability of premium assistance. Currently, Covered CA does not offer a plan that is appropriate for low-income uninsured YA population given their health costs, utilization, and health status. As of now, it appears more "financially advantageous" for lower-income young adults to remain uninsured and pay out-of-pocket than to enroll for health insurance, which may continue the trend of low insurance rates among YA.<sup>43</sup>

## Designing a Young Adult Plan: The Massachusetts Model

To design this plan, it is useful to set the stage by examining a similar idea implemented in Massachusetts. In 2006, the state of Massachusetts adopted two coverage opportunities for young adults between 19-26 years of age.<sup>44</sup> These opportunities were:

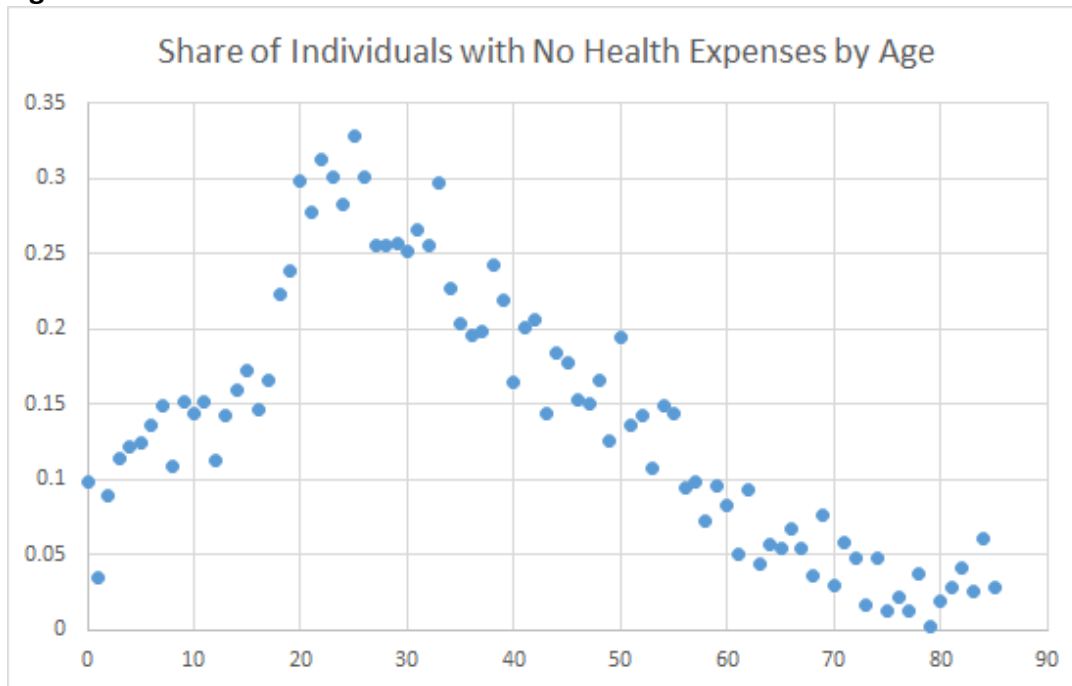
- 1) Extend eligibility for dependent coverage from 19 to 26 years of age.
- 2) Establish and offer a YA plan through the state's health insurance exchange for those who have no access to employer based coverage.<sup>45</sup>

As a result of these reforms, uninsured rates for the 19-to-26 age range dropped from 21% to 8% in two years. Furthermore, an estimated 6% of the total 13% drop in the uninsured rate was due to the Young Adult Plan alone.<sup>46</sup> Massachusetts has since ended the YA Plan in exchange for the ACA's Catastrophic Plan, which initially reversed the trend with the uninsured rate increasing to 9.2% in 2009. Since then, however, the uninsured rate has dropped to 6.2% in 2014.<sup>47</sup>

Young adult plans are more suitable for California's younger population because they would offer financial protection against catastrophic circumstances, but would have lower premiums than a traditional plan. Young adults are a "healthier-than-average" population with lower health utilization rates than other age groups.<sup>48</sup> As Figure 2 shows, 25%-30% of individuals ages 19-to-30 have *no* health expenses. This incentivizes insurance companies to offer YA a plan with lower premiums, cheaper co-pays for a limited number of visits, and protection from financial ruin. As might be expected, as a component of its initial reform, Massachusetts was able to offer the YA Plan at a lower cost than the regular metal tier plans. Table 2 shows the cost of the various plans offered.



**Figure 2**



Source: Medical Expenditure Panel Survey (MEPS), 2013

Prior to the ACA and the substitution of the Catastrophic Plan for the YA Plan in Massachusetts, the YA Plan (with Rx/prescription) was about 22% cheaper than the Bronze Plan.

California's Young Adult Plan would close the gap between the cost of foregoing coverage and paying for health insurance. If Covered CA were to offer a California Young Adult Plan (CYAP) with premiums at about 22% cheaper than a Bronze Plan, the premium prices would be \$74 per month for a 19-year-old and \$130 for a 29-year-old (see Figure 3 below).

**Table 2**

<b>Commonwealth Choice Monthly Premium Ranges by Plan Level</b>	
<b>Plan Type</b>	<b>Monthly Premium Range (August 2008)</b>
Gold	\$337–\$551
Silver	\$269–\$415
Bronze	\$193–\$287
Young Adult Plan (with Rx)	\$158–\$196
Young Adult Plan (without Rx)	\$133–\$176

\* These premium ranges represent the range in monthly premium costs among those plans available to a single 35-year-old living in the Boston area. For Young Adult Plans, the premium range represents those plans available to a single 25-year-old living in the Boston area.

Source: Lischko A., Bachman S., Vangeli A. The Massachusetts Commonwealth Health Connector: Structure and Function. The Commonwealth Fund. May 2009.  
<http://www.commonwealthfund.org/~media/Files/Publications/Issue%20Brief/2009/May/Issue%20Brief.pdf>

Prior to the ACA and the substitution of the Catastrophic Plan in place of the YA Plan, the YA Plan (with Rx/prescription) was about 22% cheaper than the Bronze Plan.

The proposed CYAP would close the gap between the cost of foregoing coverage and paying for health insurance. If Covered CA were to offer CYAP with premiums at about 22% cheaper than a Bronze Plan, the premium prices would be \$74 per month for a 19-year-old and \$130 for a 29-year-old (see Figure 3 below).

A 25-year-old would pay about \$1,553 for CYAP (premium plus three co-pays), which is lower than the \$1,770 cost of remaining uninsured (see Table 3 below).<sup>49</sup> The Massachusetts' experience provides reinforcing evidence that this policy option significantly increases affordability and provides a more appropriate plan option for young adults.

**Table 3: Cost of CYAP and Bronze Plan for a 25-year-old as Compared to Foregoing Insurance**

	Overall Expenditure	Compared to Uninsured: (\$1,770 – Cost of Plan)
CYAP	\$1,550	+ \$220
Bronze	\$2,295	- \$525

Source: Medical Expenditure Panel Survey (MEPS), 2013, and Covered CA

Finally, when assessing affordability, it is also necessary to determine if CYAP will cause any change in QHP premium prices due to risk pool alteration. Within Covered CA, 57,000 YA under 30 with incomes over 400% FPL may shift to CYAP, affecting risk pools for their previous plans. However, nearly 86,000 currently uninsured YA of the same characteristics may sign up for CYAP. This group could aid in lowering CYAP premiums.<sup>50</sup> As in all health insurance programs, if you add options, some adverse selection will occur. We think, however, the trade-offs tilt toward offering a plan for young adults.

As discussed above, offering CYAP will greatly improve affordability for this population. Given that this is the largest barrier YA face in obtaining coverage, CYAP will likely incentivize many YA to enroll. The CYAP we envision is based on Massachusetts' YA Plan, and therefore the projected enrollment will likely mirror Massachusetts' success. Recall that in two years of YAP, Massachusetts decreased its YA uninsured rate from 21.1% to 8.2%, with 6% of this drop due to YAP. This 6% rate represents a 28% drop in the uninsured rate. If CYAP experienced similar enrollment, California's uninsured rate could potentially drop from 21.5% to 15.5%. Given that California's YA population is roughly 6.4 million people, this 6% drop represents 384,000 new enrollees.

However, this comparison involves several assumptions. Massachusetts is much smaller in population, with 6.75 million people compared to California's 39 million. Additionally, California has a larger undocumented population than Massachusetts, with an estimated 420,000 undocumented YAs (6.5% of the entire YA population).<sup>51</sup> If CYAP excluded these individuals,

that could slightly lower enrollment projections, depending on the Deferred Action for Childhood Arrivals (DACA)-eligible proportion.<sup>52</sup>

Another key feature that affects CYAP's enrollment projections is the role of the so-called *endowment effect*. This phenomenon describes consumers' preference for their current state that biases them against future buying and selling.<sup>53</sup> As it applies to the YA scenario, the Massachusetts example revealed that once YA purchased health insurance, they were likely to keep it even when the reform ended and YAP was replaced by the less-appealing Catastrophic Plan.

**Table 4: Uninsured Young Adult Population**

Uninsured Rates (unadjusted)	Massachusetts			
	2005	2007	2009	2014
19 to 26 (all)	21.1%	8.2%	9.8%	6.2%
27 to 33 (all)	14.9%	8.2%	9.1%	7.0%

Source (2005-2007): State Health Access Reform Evaluation (SHARE)

Data Source (2009-2014): American Community Survey (ACS)

As depicted on Table 4, the gains achieved by the 2005-2007 health reform, including the YA Plan, were not completely lost when the reform was replaced by the ACA, which did not include a YA Plan. When the ACA was initially enacted, the uninsured rate rose from 8.2% to 9.8%, consistent our theory that the YA Plan is desirable for YA to take up. Clearly, however, the uninsured rate did not increase to anywhere near its 2005 level. This suggests that YA take-up of health insurance is influenced by the endowment effect: once they have health insurance, they are likely to keep it. Thus, the enrollment effect of CYAP are likely to be long lasting and relatively resistant to potential price increases in the future.

## **Political Feasibility**

With little to no financial downside for the state, and a projected increase in enrollment, the YA plan policy option will likely be politically attractive to the Legislature. In terms of public support, the YA demographic would be in favor of this policy option as well. A stakeholder group that may resist CYAP is Covered California's current insurance providers offering Bronze Plans. Because some YA may leave their Bronze Plans in favor of CYAP, the insurer's revenue from premiums could decrease and there could be some adverse selection which would raise costs. Overall, however, this is likely a small concern compared to the benefits of CYAP which those same insurers could offer. Since there would be no direct costs to the state budget, there should not be legislative resistance on that score.

## **Conclusions**

California has been especially proactive among the states in expanding health insurance coverage to the uninsured. We suggest three areas in which further expansion could be pursued. These are:

- 1) Allowing undocumented immigrants to purchase health plans through Covered CA without cost assistance;
- 2) Implementing a state tax penalty for not carrying insurance of 2.5% of an individual's income; and
- 3) Creating a California Young Adult Plan (CYAP) for those 19 to 30 years of age and with income > 400% Federal Poverty Level.

The first recommendation would recognize the demographic reality of California and many in the uninsured population. Since there would be no subsidy, there would be no significant fiscal implication of this proposal although its enrollment impact would be limited by cost to the individual. Our second recommendation is designed to provide an appropriate incentive for individuals to buy insurance coverage. It is important for any insurance plan to have a diversity of risks and to avoid adverse selection. Finally, a Young Adult Plan would be more attractive to a

group of individual who have low health risks but still are in need of coverage should a major illness or injury strike.

All three of these recommendations involve trade-offs. In making them we attempted to balance the benefits of health insurance with fiscal implications and political feasibility. In some cases, we took advantage of previous experience in Massachusetts to guide our analysis for California. Were California to implement these recommendations, it could also provide a model for other states.

## **List of Abbreviations in Chapter Text and Footnotes**

ACA: Affordable Care Act (aka PPACA)  
ACS: American Community Survey  
APTC: Advance Premium Tax Credit  
CA: California  
CalSIM: California Simulation of Insurance Markets  
CHIS: California Health Interview Survey  
CPI: Consumer Price Index  
CSR: Cost Sharing Reduction Subsidies  
CYAP: California Young Adult Plan  
DACA: Deferred Action for Childhood Arrivals  
FPL: Federal Poverty Level  
HHS: Department of Health and Human Services Agency  
Medi-Cal: California Terminology for Medicaid  
MEPS: Medical Expenditure Panel Survey  
PPACA: Patient Protection and Affordable Care Act (aka ACA)  
QHP: Qualified Health Plan  
SB: Senate Bill  
YA: Young Adult

## Endnotes

<sup>1</sup>A list of acronyms used in this chapter appears at the end.

<sup>2</sup>Medi-Cal is the California name for Medicaid.

<sup>3</sup>We considered other options as well but rejected them on various grounds. The original report on which this chapter is based contains those evaluations.

<sup>3</sup>Hill, L., Hayes, J. Just the Facts: Undocumented Immigrants. Public Policy Institute of California. June 2015. [http://www.ppic.org/main/publication\\_show.asp?i=818](http://www.ppic.org/main/publication_show.asp?i=818)

<sup>5</sup>Hill, L., Hayes J. Just the Facts: Undocumented Immigrants. Public Policy Institute of California. June 2015. [http://www.ppic.org/main/publication\\_show.asp?i=818](http://www.ppic.org/main/publication_show.asp?i=818)

<sup>6</sup>Hill, L., Hayes J. Just the Facts: Undocumented Immigrants. Public Policy Institute of California. June 2015. [http://www.ppic.org/main/publication\\_show.asp?i=818](http://www.ppic.org/main/publication_show.asp?i=818)

<sup>7</sup>Vargas Bustamante, A., Fang, H., Garza, J., et al. Variations in Healthcare Access and Utilization Among Mexican Immigrants: The Role of Documentation Status. *Journal of Immigrant and Minority Health*. 2012, 14(1):146-155. doi:10.1007/s10903-010-9406-9.

<sup>8</sup>Achkar, J.M., Sherpa, T., Cohen, H.W., Holzman, R.S. Differences in Clinical Presentation among Persons with Pulmonary Tuberculosis: A Comparison of Documented and Undocumented Foreign-Born versus US-Born Persons. *Clin Infect Dis*. (2008) 47 (10):1277-1283. doi: 10.1086/592572; Coritsidis, G.N., Khamash, H., Ahmed, S.I., Attia, A.M., Rodriguez, P., Kiroychewa, M.K., Ansari, N. The initiation of dialysis in undocumented aliens: the impact on a public hospital system. *Am J Kidney Dis*. 2004 Mar, 43(3):424-32.

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<sup>10</sup>Gusmano, M. Undocumented Immigrants in the United States: Demographics and Socioeconomic Status, Issue Brief. The Hastings Center. February 14, 2012. <http://www.undocumentedpatients.org/issuebrief/demographics-and-socioeconomic-status/>

<sup>11</sup>CalSIM Version 1.91 Statewide Data Book 2015-19 (May 2014)

<http://healthpolicy.ucla.edu/publications/Documents/PDF/2014/calsimdatabook-may2014.pdf>

<sup>12</sup>The living wage calculator is calculated to estimate the cost of living in communities and regions. The calculation includes typical expenses, living wage, and typical wages. <http://livingwage.mit.edu>

<sup>13</sup>McConville, S., Hill, L., Ugo, I., Hayes, J. Health Coverage and Care for Undocumented Immigrants. PPIC. November 2015. [http://www.ppic.org/content/pubs/report/R\\_1115SMR.pdf](http://www.ppic.org/content/pubs/report/R_1115SMR.pdf)

<sup>14</sup>Wallace, S. P., et al. Undocumented Immigrants and Health Care Reform. August 31, 2012. <http://healthpolicy.ucla.edu/publications/Documents/PDF/undocumentedreport-aug2013.pdf>

<sup>15</sup>Wallace, S. P., et al. Undocumented Immigrants and Health Care Reform. August 31, 2012. <http://healthpolicy.ucla.edu/publications/Documents/PDF/undocumentedreport-aug2013.pdf>

<sup>16</sup>California (State). Legislature. Senate. An act to amend Section 14007.8 of the Welfare and Institutions Code, relating to health care coverage (SB 4). October 9, 2015.

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# **CHAPTER 8**

## **Death and Resurrection: The Tale of Coroner Noguchi**

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It is doubtful that when a Los Angeles County resident is asked to name an important County public function, he or she would name the Coroner's office. Certainly, it would not be on the top of the list. Yet when someone dies from unknown causes or under suspicious circumstances, it's the County Coroner's office that does the investigating. High profile crimes that end with dead bodies involve the Coroner. When celebrity deaths are involved – and LA has no shortage of celebrities – the Coroner is likely to play a role.

Maybe we don't think about the Coroner because death is an unpleasant subject to consider. Or maybe the odd structure of LA County governance is the cause. The County is administered by five co-equal supervisors; it does not have an elected chief executive. Despite periodic suggestions that the largest county in the country needs an elected chief, the elected five supervisors seem to be reluctant – to say the least – to have such an executive official. Turnover among the five is rare, unless they are termed out. And in the past, before term limits were imposed, it was rarer still.

There are other elected LA County officials: the District Attorney and the Sheriff. It's usually these elected officials who attract the major share of public attention and name recognition. But, as will be described below, there was a time when the unelected Coroner had considerable name recognition.

In recent years, however, unless there was a problem in its administration, residents were unlikely to hear much about what went on at the Coroner's office in any detail. As it happens, 2016 was such a period. A backlog of cases was highlighted in a Grand Jury report and then-Coroner Mark Fajardo stepped down, complaining that the supervisors had underfunded his office.<sup>1</sup> Even so, public attention quickly turned elsewhere.

There was one County Coroner who maintained high visibility throughout his career from the 1960s and into the 1980s: Dr. Thomas T. Noguchi. He wrote two books about his work, mainly

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<sup>1</sup>Hillary Jackson, "LA County coroner's office could lose its accreditation," *MyNewsLA*, April 21, 2016. <http://mynews1a.com/government/2016/04/21/report-claims-la-county-coroners-office-could-lose-its-accreditation/>.

dealing with celebrity cases.<sup>2</sup> A third book he authored was a novel about a coroner dealing again with a celebrity death. One of the books became a best seller.<sup>3</sup>

Noguchi appeared in films, one being an exploitation-documentary, *The Killing of America*.<sup>4</sup> He also appeared in two related video documentaries: *Autopsy: Through the Eyes of Death's Detectives* and *Voices of Death*.<sup>5</sup> Despite his propensity for popular publicity, Noguchi's technical skills were also noted in the professional world. In 2015, Noguchi – long retired – received a special award from the American Academy of Forensic Sciences and recorded an interview reflecting on his career.<sup>6</sup>

During his career as County Coroner, critics complained that Noguchi was attempting to “steal the last scene” from Hollywood demises.<sup>7</sup> Noguchi had the distinction of being *twice* fired from his job by the Board of Supervisors, events that cemented him as a household name in LA. And his first firing ultimately triggered a community reaction, the focus of this chapter.

As the name Noguchi suggests, Thomas Tsunetomi Noguchi was of Japanese background. Unlike most of the Japanese-origin population in LA at the time, however, he had not been born in the U.S. Noguchi was born in Japan in 1927 and grew up in wartime and postwar Japan where he received his medical training. Details about his early life are scarce. But he came to the U.S. at age 25, finished his medical education, and obtained a position in the LA County Medical Examiner's (Coroner's) office.

By 1962, after only a short time on the job, he came to public attention after doing the autopsy on movie star Marilyn Monroe. After becoming Coroner in 1967, he handled the forensic aftermath of the assassination of U.S. senator and presidential candidate Robert F.

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<sup>2</sup>Thomas T. Noguchi with Joseph DiMona, *Coroner* (New York: Simon and Schuster, 1983); Thomas T. Noguchi with Joseph DiMona, *Coroner at Large* (New York: Simon and Schuster, 1985). Coauthor DiMona was a “ghostwriter” who in this case was visible. He also co-wrote with H.R. Haldeman of Watergate scandal fame.

<sup>3</sup>Thomas T. Noguchi and Arthur Lyons, *Unnatural Causes* (New York: Putnam and Sons, 1988).

<sup>4</sup>Trailer at <https://www.youtube.com/watch?v=XjwOnQktNC8>. Full film at <https://www.youtube.com/watch?v=B9Am3iPu6z8>. Noguchi can be seen at approximately the 3-minute point.

<sup>5</sup>Susan King, “VCR Viewing; For a Change, Make Your Own Discovery With 'New Explorers,'” *Los Angeles Times*, November 4, 1999.

<sup>6</sup><https://www.youtube.com/watch?v=fLTgnZfaKJs>.

<sup>7</sup>Douglas Stein, “Thomas Noguchi: Coroner to the Stars” (Interviewed November 1986): <http://web.archive.org/web/20030402115931/http://www.omnimag.com/archives/interviews/noguchi.html>.

Kennedy in 1968. As time went on, such personalities as actress Sharon Tate (victim of the Manson family), actor-comedian John Belushi, and singer Janis Joplin, among others, passed through his hands – as corpses.

In 1969, Noguchi was fired as Coroner by the Los Angeles County Board of Supervisors. His dismissal mobilized the Japanese-American community in LA. Up to that point, the community had been largely silent after returning from being placed by federal decree into internment camps during World War II. Ultimately, that community's switch in the 1970s from silence to protest led (eventually in the 1980s) to successful demands for a presidential apology and for monetary reparations by the U.S. government for the internment episode. Noguchi had been in Japan at the time of the internment and so he did not experience it. But his firing occurred at the cusp of a transition in the community from quiet to agitation.

## **Resignation**

You might think that Los Angeles County, with its current large population of about 10 million, would have an extensive public archive of historical records including records related to the Noguchi case. Alas, that is not the situation. So what we know now of Noguchi's career with the County is mainly contained in newspaper accounts and in accounts of participants. And there are missing elements and uncertainties in the record.

For example, when the promotion of Dr. Noguchi to the position of Coroner was under consideration, the proposed appointment was apparently supported by the County Employees Association, a local public-sector union. But it was reportedly opposed by the County Medical Association and the UCLA and USC medical schools. Why the opposition? Who exactly within these professional institutions did the opposing? There is nothing in the public record to explain it.



Possibly, opponents had their own favored external candidate, someone other than Noguchi, the insider.<sup>8</sup> One report indicates they viewed Noguchi as “too young and too inexperienced.”<sup>9</sup> But whatever the reason, the opposition was reflected in the Board of Supervisors vote.

Originally, two supervisors – Frank G. Bonelli and Kenneth Hahn<sup>10</sup> – supported the Noguchi appointment. Two supervisors – Burton W. Chase and Warren Dorn – opposed it.<sup>11</sup> To break the 2-2 tie, Supervisor Ernest E. Debs supported the appointment, but conditioned on Noguchi having “patched up (his) relations with the medical schools within six months.”<sup>12</sup> We know that Dr. Noguchi continued as Coroner after Debs’ six month deadline. So he presumably “patched up” his relations with the medical schools – or tried to do so. Exactly what Noguchi did in that regard is unknown, another blank spot in the historical record.

However, it is known that he faced various managerial challenges in taking over the office from his predecessor. There was a backlog of cases (as in 2016!) and there were cumbersome procedures for handling cases which needed attention. To speed up the processing, Noguchi apparently determined his office needed more funding from the County. And that is where his problems began.

Although LA County doesn’t have an elected chief executive, it does have an appointed official handling administrative affairs. That position, and the person in it, has varied in title and

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<sup>8</sup> Apparently, there were “applicants from all over the world” for the position when the incumbent coroner resigned. Source: Godfrey Isaac, *I’ll See You in Court* (Chicago: Contemporary Books, 1979), p. 55.

<sup>9</sup> Ray Zeman, “Coroner Noguchi Quits in Feud with Hollinger,” *Los Angeles Times*, February 26, 1969. This reference from the *Los Angeles Times* and others that follow are available online in the ProQuest Historical Newspapers database. Reporter Ray Zeman, who covered the initial phases of the Noguchi affair, was a longtime journalist who specialized in County and state affairs. He died in 1997 at age 86. [http://articles.latimes.com/1997-03-30/local/me-43643\\_1\\_former-times-bureau-chief](http://articles.latimes.com/1997-03-30/local/me-43643_1_former-times-bureau-chief).

<sup>10</sup> Hahn, a Democrat, was the father of James Hahn (Mayor of the City of LA, 2001-2005) and Congresswoman Janice Hahn. (She is running for a seat on the Board of Supervisors at this writing). Bonelli’s name survives in the Bonelli Regional Park. Also a Democrat, he was noted for an unsuccessful ballot proposition to give southern California additional representation in the state senate.

<sup>11</sup> Republican Chace’s name survives as Chace Park. Dorn, also a Republican, was known for efforts that helped establish the Music Center and work relating to air pollution control.

<sup>12</sup> Ray Zeman, “Coroner Faces Threat of Ouster Proceedings,” *Los Angeles Times*, February 22, 1969; Richard West, “Noguchi, New Coroner, Faces Era of Change in Department,” *Los Angeles Times*, December 26, 1976. As a state assemblyman, Debs sponsored the bill that created the UCLA Medical Center. A Democrat, Debs name survives as Debs Park. Effectively, the Noguchi appointment as Coroner was supported by the Democratic members of the Board of Supervisors and opposed by the Republicans. However, note that the office of supervisor is non-partisan.

authority over time, depending on the disposition of the Board and the degree to which the supervisors were willing to delegate. During the initial years of the Noguchi appointment, the County's chief administrative officer was Lindon S. Hollinger, who went by "L.S." or "Lin." Hollinger had been appointed to the CAO position in 1958. But he was a longtime County employee, starting as a messenger in 1925 and working his way up.

Hollinger's brother, Roscoe, had been County Auditor-Controller before retiring in 1967.<sup>13</sup> The County seemed to be a family affair for the Hollingers. CAO Hollinger was supportive of expanding LA County activities. He wrote an enthusiastic internal report on the "Lakewood Plan," an arrangement by which local cities would contract for basic services, such as policing, from the County.<sup>14</sup>

By the time Noguchi became coroner, CAO Hollinger had developed a reputation as someone who wanted ultimate control of ongoing County operations and bureaucracy and who did not appreciate anyone challenging his decisions and control. Given Hollinger's long career with LA County, he understood the way things worked from the inside. Any issue from the County bureaucracy requiring the attention of the Board of Supervisors was supposed to go through the CAO.

When Noguchi decided he needed more funding to deal with his case backlog issue, he first asked Hollinger to obtain the money for him. When Hollinger decided against provision of additional funding, Noguchi went over his head directly to the Board of Supervisors. The Board granted his request. Hollinger was upset at being bypassed and called in Noguchi for a dressing down. According to Noguchi's (second) attorney, Hollinger in fact drew his finger across his throat to indicate he (Noguchi) was finished as Coroner.

In a second interview with Hollinger, Noguchi was told there had been many complaints about him. As a result, he would have to resign. Exactly what these complaints entailed, and who had made them, was not disclosed by Hollinger at the interview. But if Noguchi resigned quietly, Hollinger said he would obtain an appointment for him at Rancho Los Amigos Hospital as chief

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<sup>13</sup>"Still in the Family," *Deseret News*, June 29, 1967, p. 6A.

<sup>14</sup>L.S. Hollinger, "The Lakewood Plan," unpublished County report, 1967. (Available from the UCLA library, Southern Regional Library Facility.)

pathologist. Noguchi apparently did resign, or at least wrote a letter of resignation. The details of whether he actually sent his letter of resignation to Hollinger privately are unclear.<sup>15</sup> But the letter was ultimately released to the public. In any case, Noguchi consulted an attorney, a friend named David S. Smith,<sup>16</sup> and was told by his friend/lawyer to withdraw the letter – which he later did.

To repeat, at this late date all we can do is speculate on motives of the parties involved. We don't know for sure why the local medical establishment opposed the Noguchi appointment as Coroner. We don't know for sure why Hollinger was unsympathetic to Noguchi's funding request, and why he denied it. But one could suspect that among these motivations was Noguchi's Japanese background. In any event, the Japanese-American community, although at first reluctant to make a fuss, eventually came to view the Noguchi affair as an affront.<sup>17</sup> By the end of the affair, it was Hollinger – not Noguchi – whose job was at risk.

### **The Battle Begins**

Once Hollinger had demanded Noguchi's resignation, and once Noguchi had (ultimately) refused, a procedure was set in motion. First the County Board of Supervisors would consider the matter of whether Noguchi should be dismissed in executive (non-public) session. If the Supervisors concurred with Hollinger's position – that Noguchi should resign or be fired – and if Noguchi still refused to resign, the matter would go to the Civil Service Commission. The Commission could ultimately dismiss Noguchi by concurring with the Board. Or it could reinstate Noguchi.

But again, exactly what happened initially is not quite clear from the newspaper accounts. First, it was indicated that Noguchi wouldn't resign. Then it was announced that Noguchi would resign after Hollinger had threatened to file "some type of charge." It was reported that Hollinger believed Noguchi spent too much time on routine deaths and not enough on violent

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<sup>15</sup>Noguchi's version of the story is that he did send the letter. (Noguchi, *Coroner*, p. 111) Noguchi's second attorney indicates that he was about to forward the letter of resignation to Hollinger but thought better of it after consulting his first attorney. (Isaacs, p. 59)

<sup>16</sup>One news account lists the name as Davis rather than David. That difference could be a typo. Ray Zeman, "Noguchi Withdraws His Resignation as Coroner," *Los Angeles Times*, March 5, 1969.

<sup>17</sup>Stanley O. Williford, "The Old Order Passes for L.A. Japanese," *Los Angeles Times*, August 24, 1969.

and suspicious cases. In any event, it can be assumed that anti-Noguchi allegations were being leaked to the news media to pressure him.

However, even when it seemed that Noguchi would resign, there would be a brief delay until March 4, 1969 before it took effect while Noguchi finished his testimony at the trial of Sirhan Sirhan, the assassin of Senator Robert Kennedy. Noguchi would receive no cut in pay and would continue as a pathologist for the County. He released a statement that *“I am fortified in my decision (to resign) by my knowledge that as coroner I have contributed to improvement of the office and its ability to service the public.”*<sup>18</sup>

However, after announcing his resignation, Noguchi confided in his dentist, Dr. Yoshio Yamaguchi, that he felt he was being treated unfairly. Dr. Yamaguchi, in turn, prevailed on a prominent attorney he knew to take over the case. On March 4, 1969, rather than step down, Noguchi officially announced that he had withdrawn his resignation. It was announced that he had hired a new attorney, Godfrey Isaac.<sup>19</sup> Isaac, it might be noted, later became a lawyer for Sirhan Sirhan after he was convicted.

In hiring Isaac, Noguchi had effectively also obtained the services of Isaac’s wife, Roena, who – although not a lawyer – provided important legal research for his case. Noguchi explained that he had changed his mind about resigning *“after I received tremendous support from my friends who know me well... I have done nothing wrong.”*<sup>20</sup> Despite the reference to friends, the only tangible support at that point was coming from Dr. Yamaguchi who began a fundraising effort for the Noguchi defense. But as time went on, the external support from the Japanese-American community would swell.

Given Noguchi’s sudden un-resignation, the Board of Supervisors suspended him and appointed an acting coroner. Although Noguchi had at first gone along with the resignation

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<sup>18</sup>Ray Zeman, “Coroner Noguchi Quits in Feud with Hollinger,” *Los Angeles Times*, February 26, 1969.

<sup>19</sup>Exactly when the switch of lawyers occurred is unclear. Another attorney, possibly a partner of Smith’s, named Manley Freid is mentioned in one account. Ray Zeman, “Noguchi Withdraws His Resignation as Coroner,” *Los Angeles Times*, March 5, 1969. Isaac died in 2015.

<sup>20</sup>Ray Zeman, “Noguchi Withdraws His Resignation as Coroner,” *Los Angeles Times*, March 5, 1969.

and then withdrew it without much detailed public explanation, his wife, Hisako Nishihara, was anything but silent.<sup>21</sup> And she immediately raised the racial issue:

*"My husband is good enough to work under a Caucasian but not good enough to work in the position of chief... There is nothing equal about this equal opportunity business if a minority group member has to have ten times more education to successfully compete against a member of the Caucasian race."*

Supervisor Kenneth Hahn, however, denied that there was any racial motivation on the part of the Board.<sup>22</sup> But after the comments of Noguchi's wife, the issue of discriminatory intent was firmly embedded in the affair.

### **The Court of Public Opinion**

If Noguchi had quietly resigned as Hollinger had wished, the entire matter would have received little public scrutiny and would soon have been forgotten. But Noguchi's resigning and un-resigning, combined with Mrs. Noguchi's statement, turned the matter into a very public event. Although the Civil Service Commission was to be the official locus for the investigation, both sides began to enlist public support by putting out their clashing views of Noguchi's fitness for office.

The formal firing by the Board of Supervisors – which triggered the Civil Service Commission hearing – took place on March 18, 1969. CAO Hollinger submitted a report charging that Noguchi took drugs, had symptoms suggesting he needed psychiatric care, was a poor administrator, and that he bullied his employees. Noguchi's attorney Isaac proclaimed in contrast that he had "full confidence that Dr. Noguchi will be returned to his position."<sup>23</sup>

Martin Weekes, LA Deputy County Counsel, was assigned to present the evidence against Noguchi. He charged that Noguchi might have made "promises" to employees of the Coroner's

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<sup>21</sup>His wife held a doctorate in microbiology. Source: Robert Lindsey, "A Chastised 'Coroner to the Stars,'" *New York Times*, March 12, 1982.

<sup>22</sup> Quotes and other material from Ray Zeman, "Noguchi Withdraws His Resignation as Coroner," *Los Angeles Times*, March 5, 1969. Supervisor Hahn stated, "His wife charges Oriental-Japanese discrimination, which it isn't."

<sup>23</sup>Richard West, "Ban on Radio, TV Reversed at Noguchi Hearing," *Los Angeles Times*, May 9, 1969.

office in exchange for their favorable testimony.<sup>24</sup> In contradiction, Noguchi's attorney Godfrey Isaac denied that anyone was "barging into (employees') houses at night." Isaac pushed to have the Civil Service Commission procedure broadcast on radio and TV, but the Commission at first rejected the idea.<sup>25</sup> The Commission's view was that broadcasting the hearings would result in a "circus."

However, the level of public interest was high by that point; the Commission soon reversed its decision, partly due to pressure from the Board of Supervisors. The Supervisors feared any indication of a secretive process. Isaac proclaimed the decision to reverse on broadcasting to be "a preservation of the democratic process." Commission President O. Richard Capen acknowledged the interest of the news media and professed "no wish to interfere with legitimate news operations."<sup>26</sup>

Capen, six years later, was himself investigated and then convicted of lying under oath and trying to fix a civil service exam. But in 1969, he was a well-respected civil servant.<sup>27</sup>

Commissioner Harry Albert was a lawyer who had been on the Commission for many years and had been with the County since at least 1931. His service on the Commission ended later in 1969.<sup>28</sup> Commissioner Thelma Mahoney succeeded Capen as President of the Commission when his service ended in 1970.<sup>29</sup> She was first appointed in 1961 after a background in the local labor movement.<sup>30</sup> The three commissioners would make the ultimate decision.

## **The Hearings Begin**

As the Commission hearings opened, Deputy County Counsel Weekes, essentially acting as prosecutor, claimed that Noguchi suffered from a "sickness" that he had developed on the job

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<sup>24</sup>Weekes retired after 32 years with the County in 1995.

<http://transparentcalifornia.com/pensions/search/?a=los-angeles-county-pension&q=martin+weekes&y=2015>.

<sup>25</sup>Ray Zeman, "Reports of Witness Tampering Heard in Noguchi Firing Case," *Los Angeles Times*, May 1, 1969.

<sup>26</sup>Richard West, "Ban on Radio, TV Reversed at Noguchi Hearing," *Los Angeles Times*, May 9, 1969.

<sup>27</sup><http://www.metnews.com/articles/2009/perspectives092909.htm>.

<sup>28</sup><http://www.upi.com/Archives/1983/07/13/Civil-Service-President-dies/9607426916800/>.

<sup>29</sup><http://dhrdcap.co.la.ca.us/jic/digest/pdf/digest1972/12221972.pdf>.

<sup>30</sup><http://dhrdcap.co.la.ca.us/jic/digest/pdf/digest1973/06291973.pdf>.

and that led him to make morbid statements.<sup>31</sup> (Readers should keep in mind, in considering the charges of morbid statements, that we are talking here about a *coroner*, i.e., someone in an occupation dealing daily with death and dead bodies, sometimes in gruesome condition.) It was alleged that Noguchi had said at the time of the Robert Kennedy shooting, that he hoped the senator would die, because his death would elevate Noguchi's reputation as Coroner. He was said to have been cheered by various aircraft disasters in the LA area that had led to substantial dead bodies to be examined. Noguchi was said to have hoped that a 727 airliner would crash into a hotel.

Weekes attempted to blunt the racial subtext of the hearing by a tactic of reversal. He claimed that Noguchi had overworked a black employee in his office who subsequently died. Noguchi was also alleged to have misbehaved with a "Japanese secretary" and a black secretary. In short, it wasn't the County that was racist. The County was in fact *protecting* minorities by firing Noguchi.

Not surprisingly, attorney Isaac had a different interpretation. Noguchi admired Robert Kennedy and would not have wished him to die. The statements about air disasters were made in the context of budget discussions, i.e., would the Coroner's office have sufficient resources to handle such catastrophes. He characterized employees who testified against Noguchi as betrayers and malingerers. One malingerer had been given a promotion after Noguchi was fired, presumably to encourage his testimony, according to Isaac. In contrast to the testimony about mistreatment of employees, Noguchi was a kindhearted and fair administrator who paid for the office Christmas party out of his own pocket. And he would never discriminate against anyone.

However, the "Japanese secretary" that Noguchi was supposed to have mistreated testified that he had told her "*he hated all niggers, he hated all Japs and he hated all Jews.*" Despite such testimony, the local Japanese-American community – which reported was at first embarrassed by the Noguchi case – had begun to rally around him. According to the *Los Angeles Times*, most of the 150 public attendees at the Commission hearings were Japanese-

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<sup>31</sup>The next few paragraphs describing the opening hearing – including the quotes – are drawn from Richard West, "Noguchi Charged with Kennedy 'Death Dance,'" *Los Angeles Times*, May 13, 1969.

Americans who “applauded politely whenever Isaac appeared to make a point in his defense of Dr. Noguchi.”<sup>32</sup> The community created an organization, JUST (Japanese United in a Search for Truth), to raise funds for the Noguchi defense.<sup>33</sup>

As the hearings continued, Noguchi was depicted by Weekes as a megalomaniac who wanted more and more power. He was reported to want to take over the Coroner’s offices in Riverside and Orange Counties.<sup>34</sup> (How this could be accomplished given the separate governance of the counties is unclear.) Indeed, Noguchi was said to dream of being in charge of all coroners’ duties west of the Mississippi while a friend of his would do everything to the east. One witness was asked to evaluate Noguchi’s “facial expression” and described him as looking “hypnotized.” Noguchi was said to have displayed a knife, saying that he would like to use it on an autopsy of CAO Hollinger while Hollinger was still alive.

Not surprisingly, the witnesses called by Isaac painted a very different picture of Noguchi. Noguchi was an expert in his field who didn’t take drugs or make bizarre or discriminatory statements. He was described as “*a warm, articulate, humane man, a leader in his community.*”<sup>35</sup> That statement was stricken from the official record as improper but, of course, it stuck in the public memory. Ultimately, with testimony largely based on alleged statements and alleged behavior, the case became a matter of credibility.

So what was to be made of testimony that Noguchi showed “joy” when bodies of Hong Kong flu victims began coming into the autopsy room? Or that his speech was sometimes “rambling”? Would the testimony of a friendly witness, a pathologist – that folks in Noguchi’s field often used morbid humor as a way of dealing with the work they faced – carry the day?<sup>36</sup>

## The Tide Turns

There were some evident problems with the case presented by the County. First there was the charge that Noguchi used some kind of “pep” pills. But no pills were ever taken directly from

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<sup>32</sup>Richard West, “Noguchi Charged with Kennedy ‘Death Dance,’” *Los Angeles Times*, May 13, 1969

<sup>33</sup>Richard West, “Noguchi’s Life Savings Gone, Backers Say,” *Los Angeles Times*, June 4, 1969.

<sup>34</sup>The next two paragraphs are based on Richard West, “Noguchi Said He Wanted More Authority, Witness Testifies,” *Los Angeles Times*, May 16, 1969.

<sup>35</sup>Richard West, “Noguchi Said He Wanted More Authority, Witness Testifies,” *Los Angeles Times*, May 16, 1969.

<sup>36</sup>Richard West, “Noguchi’s ‘Joy’ Over Influenza Autopsies Told,” *Los Angeles Times*, May 17, 1969.



Noguchi. Rather, based on testimony, the County analyzed pills that looked like pills that Noguchi was said to have taken. And even the identification of those pills did not occur until after the March 1969 Hollinger report that was the basis of Noguchi's firing. The acting coroner (perhaps in line for the permanent job if Noguchi's firing was upheld) testified that he thought Noguchi's behavior was consistent with someone taking pep pills. But no witnesses could testify that they actually had tested any pills that were known to be in Noguchi's possession.<sup>37</sup>

A psychiatrist testified for the defense that there was nothing abnormal about Noguchi. Moreover, a person who sometimes rambles is not mentally ill. And facial expressions can be misleading; witnesses who found that Noguchi smiled at what they considered inappropriate times may not have known that Japanese more often maintain a smiling expression as a matter of culture.<sup>38</sup>

Ultimately, CAO Hollinger's testimony had a major flaw in it. Given his supposed opinion of Noguchi as being mentally ill and therefore incompetent, why would he (Hollinger) offer Noguchi a job at Rancho Los Amigos hospital?<sup>39</sup> How could Noguchi be capable of taking care of the living at Rancho Los Amigos but be incapable of taking care of the dead at the Coroner's office? Hollinger admitted that he made the offer. But said he thought Noguchi could do the job, even if mentally ill.

*"Mr. Hollinger, isn't it true that you recommended the discharge of Dr. Thomas T. Noguchi because you believed he was too emotionally disturbed to perform autopsies?"*

*"Yes, that's true."*

*"Mr. Hollinger, isn't it true that when you asked Dr. Thomas T. Noguchi to resign, you offered him a post at Rancho Los Amigos Hospital as a pathologist?"*

*"Yes, I did."*

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<sup>37</sup>Richard West, "Doctor Links Noguchi Actions to 'Pep Pills,'" *Los Angeles Times*, May 21, 1969.

<sup>38</sup>Richard West, "Noguchi's Attorney Assails Procedures in Pill 'Test,'" *Los Angeles Times*, May 20, 1969.

<sup>39</sup>Richard West, "Hollinger Tells of Hospital Job Offer to Noguchi," *Los Angeles Times*, May 24, 1969.

*"Mr. Hollinger, would you tell this commission why you were ready to assign a man that was too ill to operate on dead bodies to a place where he'd be performing services for people who are still alive?"<sup>40</sup>*

While the Rancho Los Amigos offer was a major hole in the case against Noguchi, there were still other matters raised by attorney Isaac. Hollinger had blocked delivery of a new County car for Noguchi prior to his having undertaken the investigation that had led to the March report. Didn't that fact suggest he was planning to fire Noguchi even before the evidence to do so was obtained? (Hollinger said he blocked a new car because it wasn't needed, although the car Noguchi was using was four years old and had 70,000 miles on it.)

Didn't Hollinger decide to fire Noguchi when Noguchi went over his head and obtained more funding from the Board of Supervisors directly? (Hollinger denied it.) Didn't Hollinger make a slashing gesture across his throat when he confronted Noguchi and told him to resign? (Hollinger denied doing so.) Didn't one of the witnesses the County called against Noguchi then apply for a job in the CAO's office? (Hollinger admitted he did so, although the witness applied through one of Hollinger's deputies.)

One of the charges against Noguchi had alleged incompetence in his handling of the Robert Kennedy autopsy. But after the Hollinger testimony, the County asked that the Kennedy charge be dropped. That request – which the Commission granted – meant the Commissioners should ignore prior testimony that Noguchi had mishandled the Kennedy case. Attorney Isaac charged that the County was trying to prevent evidence being presented as to what an excellent job Noguchi had actually done. Nonetheless, the dropping of the Kennedy matter showed that "the County's case is dissolving in front of their eyes," Isaac said.<sup>41</sup> And Isaac was able to force Weekes to declare for the record – after hours of haggling, according to Isaac – that the autopsy of Kennedy was "competent."<sup>42</sup> So the County had brought a charge it knew to be false.

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<sup>40</sup>Quoted in Godfrey Isaac, *I'll See You in Court* (Chicago: Contemporary Books, 1979), p. 91.

<sup>41</sup>Richard West, "County Withdraws One Count Against Noguchi," *Los Angeles Times*, May 27, 1969.

<sup>42</sup>Godfrey Isaac, *I'll See You in Court* (Chicago: Contemporary Books, 1979), pp. 84-85.

## From Defense to Offense

After Hollinger's dubious testimony and the withdrawal of the Kennedy charge, the County's case did indeed begin to melt. Supervisor Kenneth Hahn – who was called by Isaac to testify – noted that if the charges against Noguchi were not substantiated, it would be Hollinger – not Noguchi – who would “be in a most difficult position.”<sup>43</sup> Indeed, if Noguchi were exonerated, charges might also be filed against those who brought the charges against him, according to Hahn.

But Hahn was anything but a friendly witness and accused Isaac of “getting publicity” with his questions. Hahn basically put the onus – if indeed there had been a wrong decision on Noguchi – on CAO Hollinger. He said that he initially had no reason to doubt Hollinger's view that Noguchi was dangerous. Yet he admitted that he (Hahn) was willing to go along with a private resignation of Noguchi that would put him into another County hospital.<sup>44</sup>

The “Japanese secretary” who testified against Noguchi admitted that she cried when it appeared he was being pushed to resign.<sup>45</sup> Yet apart from attributing racist statements to him, she had also testified that Noguchi had threatened to kill County officials and to kill her. She also accused him of using profanity, although it appears that the offensive language in question was “Hell” and “damn.” How credible a witness could she be when first she cried and then she accused? A dentist testified that the pills the County had identified as “pep pills” were probably vitamin B he had recommended.<sup>46</sup> There was more testimony put in evidence that coroners are prone to make morbid jokes. And so it went.

The withdrawal of the Kennedy charge was also a breakthrough for support of Noguchi by the Japanese-American community. Dropping one charge suggested other aspects of the case might not be solid. A big fundraiser/dinner was held for the Noguchi defense by the JUST organization in a large hall. But despite the hall's size, many Noguchi supporters had to be

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<sup>43</sup>Richard West, “Hollinger Reputation Involved in Noguchi Hearing, Hahn Says,” *Los Angeles Times*, May 30, 1969.

<sup>44</sup>Richard West, “Hollinger Reputation Involved in Noguchi Hearing, Hahn Says,” *Los Angeles Times*, May 30, 1969. Apparently, by the time the matter had gotten to Hahn and the rest of the Board, the target hospital had switched from Rancho Los Amigos to Harbor General.

<sup>45</sup>Richard West, “Aide's Fear of Resignation by Noguchi Told,” *Los Angeles Times*, May 29, 1969.

<sup>46</sup>Richard West, “Civil Service Board Dismisses Five Charges Against Noguchi,” *Los Angeles Times*, June 3, 1969.

turned away for lack of capacity. In the view of the community, Noguchi had switched from being a potential embarrassment to an obvious victim of a discriminatory decision that had to be reversed.<sup>47</sup>

By early June, the Civil Service Commission had dropped still another five charges. It was no longer to be charged that Noguchi prayed for a crash of Mayor Sam Yorty's helicopter, that Noguchi wanted great tragedies to occur to enhance his reputation, that Noguchi had made fun of a disabled person in his office, that Noguchi had changed topics to something irrelevant in the midst of a meeting, and – as noted above – that he used profanity.

Isaac wanted to rebut the idea that Noguchi was a racist. To do so, he called as a witness City Councilmember Tom Bradley. Bradley, an African-American former police officer in the Los Angeles Police Department, had run for mayor in a bruising campaign in 1969 and lost, after incumbent Yorty had hinted that Bradley was a front for black radicals. The Bradley testimony – which came only a week after the mayoral election – was held after the 1965 Watts Riots and thus in a period when racial tensions were still high in Los Angeles. But Bradley was a recognized leader of the black community; his testimony would be important.<sup>48</sup> (Bradley went on to defeat Yorty in 1973.)

Councilmember Bradley could not testify directly on allegations about what might have been said within the Coroner's office. But he did testify that he supported reforms in procedures advocated by Noguchi and that Noguchi had been "lucid" (not crazy) in a lengthy meeting that Bradley had had with him. The simple fact that Bradley was testifying for Noguchi – the subject was not important – was an indirect way of combatting the racial allegations. Isaac also called three black employees of the Coroner's office who testified that Noguchi was an excellent manager. And he called executive of a black-oriented radio station who testified that Noguchi favored making inquest procedures more open to minorities.<sup>49</sup>

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<sup>47</sup> Godfrey Isaac, *I'll See You in Court* (Chicago: Contemporary Books, 1979), pp. 88-89.

<sup>48</sup> Bradley came in first in the primary but lost in the general election. See <https://www.youtube.com/watch?v=tnDjQ1QbWho>. On the 1973 mayoral election in which Bradley won, see <https://www.youtube.com/watch?v=Val48Xn8UrY>.

<sup>49</sup> Richard West, "Noguchi Coherent, Lucid at Meeting, Bradley Testifies," *Los Angeles Times*, June 5, 1969.

Finally, there was testimony that Noguchi had calmed a tense confrontation with black “militants” who could not get into an inquest hearing regarding the police shooting of a Black Panther member. The witness – a statistical clerk in the Coroner’s office – contradicted testimony that Noguchi had misbehaved poorly at a retirement dinner. In fact, at the dinner, Noguchi had been the target of a racist joke by a TV actor who alluded to Pearl Harbor and said “*if this had been 1941, Dr. Noguchi would have come and shot the Hell out of us.*” Noguchi had responded to the remark gracefully.<sup>50</sup>

In short, the offensive mounted by Isaac was going well. But there remained one potential danger point. Noguchi wanted to testify in his own defense – something he was not required to do. Indeed, it had been affirmatively announced that Noguchi *would* testify on his own behalf, an event that would have been a climax for the defense’s case. Pulling out and not testifying might look bad. But attorney Isaac feared that Noguchi would not make a good witness for himself.

Isaac viewed any hesitancy in responses by witnesses to questions as dangerous to their perceived credibility. Noguchi’s native language was not English and he often did hesitate while searching for a word. To the Commission, that hesitancy might seem like evasion or equivocation. In the end, Isaac announced at the last moment that Noguchi would not testify after all and then closed the case. The explanation given to the news media is that Noguchi, were he to testify, would have to say unpleasant things about those in the Coroner’s office who testified against him which would be bad for morale.<sup>51</sup> Isaac told the news media that Noguchi didn’t want “the cheap success which would come from castigating a handful of his subordinates.”<sup>52</sup>

Despite the explanation, according to Isaac’s later account, when the announcement of no testimony by Noguchi was made, “*pandemonium broke out. The hearing room exploded. People jumped up shouting. Some were angry. Some were hostile. The three commissioners*

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<sup>50</sup>Richard West, “Noguchi Averted Racial Trouble, Witness Claims,” *Los Angeles Times*, June 7, 1969.

<sup>51</sup>Godfrey Isaac, *I’ll See You in Court* (Chicago: Contemporary Books, 1979), pp. 92-96.

<sup>52</sup>Richard West, “Noguchi Decides Not to Testify in Dismissal Hearing,” *Los Angeles Times*, June 10, 1969.

*were visibly upset. Weekes was red in the face, furious, yelling at me.*"<sup>53</sup> Would the decision up-end a case that seemed to be going well for Noguchi up to that point?

Isaac couldn't be sure at the time if he had made the right decision. Supervisor Kenneth Hahn – even after the Commission had heard all the evidence and had retired to consider its verdict – pushed for a reopening of the case on the grounds that Noguchi hadn't testified. In Hahn's view, there was "still confusion and a cloud" over Noguchi's fitness, without his testimony.<sup>54</sup>

## **Wrapping Up**

After the shock and letdown that accompanied the decision not to have Noguchi testify, the hearings went on in much the same way they had gone before. A UCLA psychologist diagnosed Noguchi as manic-depressive based on tests that had been administered to him, although he never met Noguchi.<sup>55</sup> The dean of the USC School of Public Administration also testified about Noguchi's alleged manic-depressive tendencies based on the tests, although he was not a psychologist. But he was tripped up by Isaac in not knowing a technical psychological term and ended up complaining about being cross-examined.<sup>56</sup>

There was testimony that the African American employee who was alleged earlier to have died from being overworked by Noguchi in fact had died of cancer. The acting coroner – who replaced Noguchi – refused, however, to say that the cause was cancer and instead said he died of respiratory failure – but acknowledged that an embolism and a malignant tumor were present. Another witness, a coroner from Detroit said explicitly the cause was a cancer that had spread to the brain.<sup>57</sup> There was also testimony to the effect that morale in the Coroner's office had declined following Noguchi's dismissal.<sup>58</sup>

In his closing argument, attorney Isaac depicted LA County as a huge giant attacking a lone individual. CAO Hollinger had become an egotistical autocrat. The anti-Noguchi witnesses were acting out of jealousy and other bad motives. Among the witnesses who made false

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<sup>53</sup> Godfrey Isaac, *I'll See You in Court* (Chicago: Contemporary Books, 1979), p. 95.

<sup>54</sup> William Endicott, "Noguchi Backers Charge Hahn with 'Sabotage,'" *Los Angeles Times*, July 22, 1969.

<sup>55</sup> Richard West, "Noguchi Personality Syndrome Brought Out by Psychologist," *Los Angeles Times*, June 11, 1969.

<sup>56</sup> Richard West, "USC Dean Blasts Procedure at Noguchi Dismissal Hearing," *Los Angeles Times*, June 13, 1969.

<sup>57</sup> Richard West, "Noguchi Testimony Focuses on Petition Urging His Retention," *Los Angeles Times*, June 14, 1969.

<sup>58</sup> Richard West, "Former Noguchi Aide Quits, Blames Decline in Morale," *Los Angeles Times*, June 24, 1969.

statements, according to Isaac, was the acting coroner who had conspired with others to come up with the pep pill story. Obviously, the County's attorney did not see things that way. The County, from his perspective, had acted to protect the "little people" who had a right to expect an efficient Coroner's office.<sup>59</sup>

Testimony and hearings had started in mid-May and ended in late June after seven weeks, although originally a much shorter proceeding had been expected. The Commission adjourned to consider the evidence with no set date to produce a decision. It had developed a reported 3,000 pages of testimony from about 80 witnesses for the commissioners to ponder. Noguchi simply said at the end that he was "available to return to public service."<sup>60</sup>

### **The Verdict**

While the Commission deliberated, the Japanese-American community through the JUST organization continued its campaign to exonerate Dr. Noguchi. A petition scroll with 7,000 names was sent to the Civil Service Commission and the Board of Supervisors.<sup>61</sup> A full-page ad was placed in the *Los Angeles Times* on Noguchi's behalf by JUST. It was entitled "A Plea for Justice" and noted that "never has the Japanese American community been more aroused."<sup>62</sup> Below the title, the subtitle warned that "if this happened to one of us, it can happen to one of you," and the text then went on to list a series of injustices to Noguchi.

While it appeared that the case had ultimately gone well for Noguchi, no one could be sure what the Civil Service Commission would decide based on the evidence presented. While Los Angeles waited, actor George Takei, who played Sulu on the original *Star Trek* TV show, and others prominent in the Japanese-American community, took issue with the efforts by Supervisor Hahn to reopen the case.<sup>63</sup> But it remained unclear when a decision would be announced.

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<sup>59</sup>Richard West, "County Pictured as Monster at Noguchi Hearing," *Los Angeles Times*, June 24, 1969.

<sup>60</sup>Richard West, "Noguchi Lawyer Accuses Four Witnesses of False Testimony," *Los Angeles Times*, June 25, 1969.

<sup>61</sup>Ray Zeman, "7,000 Sign Scroll, Ask Just Ruling on Noguchi Dismissal," *Los Angeles Times*, July 16, 1969.

<sup>62</sup>*Los Angeles Times*, July 11, 1969, p. B5.

<sup>63</sup>William Endicott, "Noguchi Backers Charge Hahn with 'Sabotage,'" *Los Angeles Times*, July 22, 1969.

Then it was announced that the Commission would issue its ruling on July 31, 1969. Attorney Isaac prepared two statements – one if Noguchi were cleared and one if the firing were upheld. On July 31 in a crowded hearing room, Commission President Capen delivered the verdict:

*“We the Civil Service Commission of Los Angeles County, after hearing over one million words in over six weeks of testimony, find that not one charge against Dr. Thomas T. Noguchi has been proven. He is reinstated forthwith as Los Angeles County Chief Medical Examiner-Coroner and awarded full back pay.”*<sup>64</sup>

The Commission did recommend that the duties of the Coroner be divided between medical and managerial. But such a reorganization was not something the Commission could order; it would require an action by the Board of Supervisors. And the Board, particularly those who voted to fire Noguchi, had had enough of the affair and were unlikely to undertake such a restructuring. Doing so would be perceived as a vendetta against Noguchi. Supervisor Debs said there needed to be a “cooling off period.”<sup>65</sup>

Following the verdict, Noguchi walked the few blocks from the hearing room to his former – and now regained – office and sat down in his old chair. The now-displaced acting coroner who had testified against Noguchi, along with other hostile witnesses/employees were out of the office on vacation or otherwise elsewhere. They subsequently requested transfers or resigned.<sup>66</sup> One was subsequently prosecuted for having a fake medical degree.<sup>67</sup> Supportive employees meanwhile welcomed Noguchi back.

CAO Hollinger – out of town on his honeymoon when the verdict came down – maintained the charges he had brought against Noguchi were valid, despite the Commission’s decision. Hollinger, whose own job was now potentially in question given the outcome, denied that he planned to retire the next year, despite reports circulating that he would do so. And the next

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<sup>64</sup>Quoted in Godfrey Isaac, *I’ll See You in Court* (Chicago: Contemporary Books, 1979), pp. 97-98.

<sup>65</sup>Paul Houston and Stanley O. Williford, “Noguchi Cleared and Reinstated to Coroner Post,” *Los Angeles Times*, August 1, 1969.

<sup>66</sup>Paul Houston, “Hollinger Still Feels Charges Against Noguchi Are Factual,” *Los Angeles Times*, August 5, 1969.

<sup>67</sup>William Farr, “Deputy Coroner Arrested as Imposter with Fake Degree,” *Los Angeles Times*, February 3, 1972.



year, he in fact did step down.<sup>68</sup> Despite Hollinger's insistence to the contrary, Civil Service Commission Capen, in response to a reporter's question, clarified the verdict's meaning. It wasn't just that the charges against Noguchi were unproved, he responded. *"The fact that (Noguchi) was restored to his job is indicative that he was exonerated."*<sup>69</sup> (Underline added.)

### A Shift in Attitude

At the time of the Noguchi affair, the civil rights movement was in full swing; other protest movements were also active. There was growing opposition to the Vietnam War, and there was "women's lib." But even with such examples, the Japanese-American community had at first been reluctant to become involved aggressively in the Noguchi case, despite the suggestion early on that a discriminatory motive for the firing was involved.

Harry Kitano, a UCLA professor, 30 years later co-authored a book on the movement for an apology and reparations for the World War II internment of the West Coast Japanese-origin population.<sup>70</sup> But at the time of the 1969 verdict, Kitano reacted to the eventual support of the Japanese-American community for Noguchi:

*"It really is a dramatic change. Very few would have predicted it. I would say that had this happened ten years ago (the community) would have acquiesced. However, this is the first time the Japanese have been in such publicly visible positions... I once said that if a wartime evacuation situation occurred again, the majority of the Japanese would merely go again. That was three years ago. After this incident I'm not so sure. The vast majority might try to resist."*<sup>71</sup>

The creator of the JUST name for the fund raising organization, Mrs. Kats Kunitsugu, elaborated:

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<sup>68</sup>Ray Zeman, "Hollinger Job Secure Despite Failure to Have Noguchi Fired," *Los Angeles Times*, August 10, 1969. Hollinger had indicated he would resign several months before the Noguchi case was presented to the Board of Supervisors. He then reversed the retirement decision after the death of his first wife, still before the Noguchi case was filed.

<sup>69</sup>Paul Houston, "Hollinger Still Feels Charges Against Noguchi Are Factual," *Los Angeles Times*, August 5, 1969.

<sup>70</sup>Mitchell T. Maki, Harry H.L. Kitano, and S. Megan Berthold, *Achieving the Impossible Dream: How Japanese Americans Obtained Redress* (Urbana and Chicago: University of Illinois Press, 1999).

<sup>71</sup>Stanley O. Williford, "The Old Order Passes for L.A. Japanese," *Los Angeles Times*, August 24, 1969.

*“The Japanese are bred to respect authority. They hate to express ill feeling against constituted authority. The formation of JUST then was quite a phenomenon. I feel that recently with the Black Power movement and the Brown Berets, the Japanese community has been standing off to the side and has not been involved. They have been learning. The Japanese don’t like to picket and carry signs. But they learn that in these times quiet people aren’t going to be heard. There is a feeling that it is no longer the right thing to do by staying quiet.”<sup>72</sup>*

Of course, the civil rights movement and others would have been examples even if there had been no Noguchi firing. So surely, pressure for an apology and reparations for the World War II internment would have come about. The book on the apology/reparations movement co-authored by Kitano mentioned above does not go into the Noguchi case or even mention it. But the book does suggest that a shift in attitudes within the Japanese American community was taking place. It dates the period of relative postwar/post-internment quiet as ending in 1969 – the date of the Noguchi affair – and the new era of more activism beginning in the 1970s. So perhaps the community support for Noguchi was a symptom of the larger shift in attitudes.

All we can say is that the Noguchi firing and hearing did come along at a critical point in time and that it created a cause around which the Japanese-American community in Los Angeles could rally. Before the Noguchi firing in 1969, there wasn’t a highly visible rallying event – other than the internment episode itself – and not much was being said about that in the post-World War II period. After 1969, there was a more activist stance.

As time went on in the 1970s, there began to be more general public awareness about the history of unjust events of all types. A dramatic TV movie about the internment, *A Farewell to Manzanar*, was shown in prime time in 1976.<sup>73</sup> *Roots* – a 1977 TV mini-series – focused on black slavery in the U.S. The following year *Holocaust* – about the Nazi extermination of

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<sup>72</sup>Stanley O. Williford, “The Old Order Passes for L.A. Japanese,” *Los Angeles Times*, August 24, 1969. The JUST name was unveiled in an article in a Japanese-American community newspaper by Mrs. Kunitsugu.

<sup>73</sup><https://www.youtube.com/watch?v=w7GN6kvmGZ0>.

European Jews – appeared as a TV mini-series. So the popular background for the enactment of a bill in the 1980s that provided an apology and reparations for the internment was being established.

## Aftermath

In any event, by the 1980s, it appears that the Japanese-American community in LA had moved on from the defense of a single individual to the apology/reparations issue for the larger group. In 1982, there were complaints about Noguchi – which seem to be perennial when it comes to the Coroner's office regardless of who is heading it – that the office wasn't being managed well and that there was a case backlog. In its 1969 verdict, the Civil Service Commission had recommended dividing the leadership of the office between a medical expert on the forensic science side and a professional manager on the administrative side. But the Supervisors never reorganized the office in that fashion. Maybe it would have been (would still be?) a good idea.

More significantly, the Hollywood establishment was annoyed with Noguchi's high profile presence when celebrity deaths were involved.<sup>74</sup> The Screen Actors Guild, complained to the Board of Supervisors about Noguchi's handling of the Natalie Wood and William Holden cases. Both were situations in which excessive drinking appeared to be a factor in the accidental deaths of the two movie stars.<sup>75</sup> Noguchi's justification for discussing drinking in the context of those cases was that he wanted to educate the public so that the living would learn from the dead.<sup>76</sup> However, there is an old Latin saying, *De mortuis nihil nisi bonum* (of the dead say nothing but good). Saying the departed drank too much wasn't saying "good."

The Board of Supervisors in 1982 once again removed Noguchi from the Coroner position. It first suspended, and later demoted, him. Hearings were again televised, as in 1969.<sup>77</sup> Noguchi

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<sup>74</sup>Noguchi was said to be the model for a coroner hero of a popular TV series in the 1970s and early 1980s: *Quincy*. "Los Angeles Coroner Faces an Investigation," *New York Times*, December 30, 1981.

<sup>75</sup>Cecilia Rasmussen, "High Profile Twice Cost 'Coroner to the Stars' His Job," *Los Angeles Times*, January 16, 2005; Robert Lindsey, "A Chastised 'Coroner to the Stars,'" *New York Times*, March 12, 1982.

<sup>76</sup>Thomas T. Noguchi with Joseph DiMona, *Coroner at Large* (New York: Simon and Schuster, 1985), p. 248.

<sup>77</sup>The County hired a well-known outside attorney – William Masterson – to handle the litigation rather than use an insider as in 1969. Masterson later became a noted judge.

blamed Proposition 13-related funding problems for administrative deficiencies.<sup>78</sup> He remained in County employ after his demotion as a physician-specialist in the Coroner's office and also had an appointment with USC.<sup>79</sup> Appeals were filed – with Godfrey Isaac again as Noguchi's lawyer. The case moved from the Civil Service Commission, which this time did not countermand what the Supervisors had done,<sup>80</sup> to the courts, and eventually to the state Supreme Court in 1987.<sup>81</sup> In the end, the Supreme Court did not reverse the demotion and Noguchi was not reinstated.

Noguchi definitely had some outside public support at the time of the 1982 demotion, in part because he had made himself a popular personality. The racial issue was raised by Isaac again, but this time it was met with some skepticism. It couldn't be denied that Noguchi had developed an image as "coroner to the stars." Moreover, there were major deficiencies in the administration of the Coroner's office that had been described in a *Los Angeles Times* investigation.<sup>82</sup> The *Times'* investigation is what triggered the Board of Supervisors' action. Noguchi himself graded his administrative work (as opposed to his medical work) as only a seven on a scale of ten.<sup>83</sup> And he was not by that point a self-deprecating person.

Thus, in this second Noguchi case – where anti-Japanese animus did not seem to be the issue – a community outcry did not result, certainly not to anywhere near the degree that had occurred in 1969. That pattern has persisted in Los Angeles. In 2016, for example, Japanese-

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<sup>78</sup>Proposition 13 of 1978 drastically cut local property taxes. Thomas T. Noguchi with Joseph DiMona, *Coroner* (New York: Simon and Schuster, 1983); Thomas T. Noguchi with Joseph DiMona, *Coroner* (New York: Simon and Schuster, 1983), p. 245.

<sup>79</sup>Noguchi's salary was reported to be higher in his demoted position than as Coroner. Dan Morain, "Supreme Court Refuses to Reinstate Noguchi," *Los Angeles Times*, March 12, 1987. He retired from County employment in 1999 but continued with USC.

<sup>80</sup>Sara Adler, a hearing officer of the Civil Service Commission, recommended reinstatement of Noguchi. However, she found significant deficiencies in the administration of the Coroner's office. The full Commission reversed the ruling, based on those deficiencies. In the litigation that followed, Noguchi's attorney claimed there was a conflict of interest because Adler's husband worked at a law firm used by the County (although Adler had issued a ruling *favorable* to Noguchi's retention as Coroner). The court rejected the conflict of interest claim. *Noguchi v. Civil Service Com.* (1986), Court of Appeals of California, Second Appellate District, Division Seven. December 12, 1986. <http://law.justia.com/cases/california/court-of-appeal/3d/187/1521.html>.

<sup>81</sup>The County operated with an acting Coroner during the litigation. After the decision of the state Supreme Court, the acting Coroner was officially appointed as Coroner.

<sup>82</sup>Investigative reporter Laurie Becklund, who died in 2015, wrote most of the stories that triggered the Supervisors' actions.

<sup>83</sup>Thomas T. Noguchi with Joseph DiMona, *Coroner* (New York: Simon and Schuster, 1983), pp. 242-243.

American Paul Tanaka – the former undersheriff of LA County and mayor of Gardena – was sentenced to five years in prison for obstruction of justice along with other top officials in the Sheriff's Department. But there was no suggestion that the Tanaka prosecution was discriminatory, and no community reaction developed to oppose it.

The tale of Coroner Noguchi, Episode 1, became a larger cause, and an injustice was reversed as a result. But Noguchi, Episode 2, was ultimately seen as just a personnel matter, albeit one involving the high profile coroner to the stars.

# **Chapter 9**

## **Undocumented Lawyer: Admission to the California State Bar**

**Stanley M. Paul**

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## Introduction: On Becoming a Lawyer in California

Every year in California thousands of aspiring lawyers take and pass the three-day California Bar exam administered by the Committee of Bar Examiners (CBE). The exam is one of the requirements to admission to the State Bar of California and to becoming a practicing attorney in this state.<sup>1</sup> Among other requirements for becoming an attorney in California – and included in California’s Business and Professions Code – are: being at least 18 years old and of “good moral character.” In addition, a test of the Rules of Professional Conduct is required along with certain educational requirements/options enumerated in the code.<sup>2</sup>

The State Bar of California, founded in 1927, is the administrative and regulatory agency of the California Supreme Court.<sup>3</sup> And, as such, the privilege to practice law in California requires membership in the State Bar. Under section 6064 (a) of the Business and Professions Code, “Upon certification by the examining committee that the applicant has fulfilled the requirements for admission to practice law, the Supreme Court [of California] may admit the applicant as an attorney at law in all the courts of this state...”

Thus, after an applicant is deemed qualified, i.e., “fulfilled the requirements,” the State Bar submits the applicant for admission by California’s highest court, and, if accepted, the court (which it routinely does) “...may direct an order to be entered upon its records to that effect,” and, “a certificate of admission thereupon shall be given to the applicant by the clerk of the court.”

However, prior to 2014, Section 6064 did **not** contain the following language, which became effective Jan. 1 of that year:

“(b) Upon certification by the examining committee that an applicant who is not lawfully present in the United States has fulfilled the requirements for admission to practice law, the Supreme Court may admit that applicant as an attorney at law in all the courts of this state...”

The history of this small recent addition taken from court records and news accounts illuminates the complex nature and functioning of not only our multifaceted state, but its intersection with federal law.

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<sup>1</sup>For numbers admitted to the California State Bar in California since 1885, go to: <https://members.calbar.ca.gov/search/demographics.aspx>.

<sup>2</sup>See California Business and Professions Code, Section 6060-6069 on Admission to the Practice of Law which may be found online at: [http://leginfo.legislature.ca.gov/faces/codes\\_displayText.xhtml?lawCode=BPC&division=3.&title=&part=&chapter=4.&article=4](http://leginfo.legislature.ca.gov/faces/codes_displayText.xhtml?lawCode=BPC&division=3.&title=&part=&chapter=4.&article=4).

<sup>3</sup>For more information on the State Bar of California, visit: <http://www.calbar.ca.gov/Home.aspx>.



This chapter, while primarily tracing the path of just one applicant's decades-long journey from "not lawfully present in the United States" to practicing attorney at law in California, also is about one who came before him and uncertainty for others that have and will come after. It is also about the role and intricate intersection of state law, the federal law, California legislation and administration. Important as well is the rule and jurisdiction -- under the California Constitution of the state's highest court -- to make policy relating to admission to the State Bar in making one individual's lifelong dream and those that follow to participate in the life of the law in California.

### **Not Lawfully Present in the United States**

In 2009, the State Bar of California records that 6,641 people were admitted to the California Bar. Among those passing the bar exam that year was Sergio C. Garcia, who graduated from high school and college in California and went on to earn his J.D. (Juris Doctorate), or law degree, from Cal Northern School of Law in Chico, California. However, Garcia was born in Mexico in 1977 and brought to California when he was 17 months old.

At the age of nine, he returned to Mexico with his family and did not return to California until he was 17.<sup>4</sup> Garcia's father, who had obtained lawful permanent resident status in California, filed an immigration visa petition for his son in 1995. But due to a backlog of persons of Mexican descent applying for visas, a visa number for Garcia was still unavailable to him nearly 20 years (the time of the court's opinion) after the original filing.

Garcia had indicated his immigration status as "pending" on his California State Bar application for determination of moral character in 2009.<sup>5</sup> As a result, while the Committee of Bar Examiners submitted his application to the California Supreme Court, it notified the Court of his status in the United States. The Committee also informed the Court that Garcia's case was one of "first impression, as we are not aware of any other jurisdiction that has ever knowingly admitted an undocumented alien to the practice of law."<sup>6</sup>

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<sup>4</sup>The details of this case are recounted in the court's opinion cited as 58 Cal. 4th 440 and 165 Cal. Rptr. 3d 855 and can be read via LexisNexis (public access to older cases in the California California courts are directed to and available via this site) at: <http://www.lexisnexis.com/clients/CACourts/> or <http://scocal.stanford.edu/opinion/re-garcia-admission-34284> or may be accessed as a pdf at: <http://www.courts.ca.gov/documents/S202512.PDF>. The case is also summarized in the Jan. 2, 2014 California Courts press release, "California Supreme Court Admits Undocumented Immigrant to State Bar," at <http://www.courts.ca.gov/24673.htm>.

<sup>5</sup>The State Bar began including questions about immigration status in 2008. See footnote 4 of the main case.

<sup>6</sup>Terms such as "alien," "immigrant," "illegal" and "unlawful" are discussed in footnote 1 of the main case as well as in the concurring opinion to this case which will be discussed later in this chapter. Quotes appearing in this chapter are from the main case authored by California Supreme Court Chief Justice Tani Cantil-Sakauye, unless otherwise indicated.

Based on this information, the Committee was instructed to show cause before the Court as to why the motion should be granted. It also listed several issues that the Committee would have to address in making its case. Included was the relevance of a federal statute that, in general, stood in the way of granting a license to practice law to an undocumented immigrant.<sup>7</sup>

At the same time numerous *amici curiae*, or “friends of the court” briefs on behalf of Garcia and the issues at hand were submitted to the Court, including one by then California State Attorney General Kamala D. Harris.<sup>8</sup> However, the court noted that a small number of briefs, including from the United States Department of Justice, included a series of general objections, which the court addressed in making its 2014 decision.

### **The Federal Statute**

Responding to Garcia’s application, the Court directed the State Bar to address a number of questions. The first concerned a federal law, Title 8 of the United States Code (U.S.C.) section 1621 that contains subdivisions (a-d).<sup>9</sup> In short, subdivisions (a-c) would effectively bar anyone in Garcia’s position (i.e., he did not fall under any of the exceptions listed in subdivision (a) from obtaining a “State or local public benefit,” – including a “professional license” by an “agency of a State or local government.” The Court noted that both Garcia and the CBE argued in their respective responses that this provision would not apply to a license issued by the Court (a distinction which plays an important part later in the story). There is also section 1621(d), that provides one important exception or available workaround; it allows for the enactment of a state law that “affirmatively provides for such eligibility.”

However, prior to 2014 there existed no such state law in California. A 2012 article in the *Los Angeles Times* quoted a legal expert as saying, “I think existing federal law makes it very problematic for him to get a license to practice law.” The article noted that it would be illegal for anyone to hire Garcia as a lawyer and that the court would be unlikely to rule in his favor.<sup>10</sup>

At the time, this view was an accurate assessment of the situation in California given section 1621 subdivisions (a) through (c). The article also noted that there were similar cases in New York and Florida. And, the opinion noted, one California applicant did fall under an exception under 1621 (a), due to receiving asylum (one of the enumerated exceptions) in the United

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<sup>7</sup>The order may be read at: <http://www.courts.ca.gov/documents/5-16-order-issuing-OSC.pdf>

<sup>8</sup>*Amici curiae* briefs may be viewed at: <http://www.courts.ca.gov/18822.htm>

<sup>9</sup>Some space in the opinion is taken up to point out that under the Supremacy Clause of the U.S. Constitution, federal law prevails over state law (U.S. Const. art. VI, cl. 2) and furthermore over immigration issues.

<sup>10</sup>Paloma Esquivel, “Undocumented Chico man passed the bar, but can he practice law,” *Los Angeles Times*, June 11, 2012. Available at <http://articles.latimes.com/print/2012/jun/11/local/la-me-sergio-garcia-20120611>

States, and was granted a license. In addition, another California applicant's case was being "held in abeyance" pending the outcome of this case (Garcia's) of first impression.

### **The California Legislation**

In September 2013, a bill pending in the California Assembly (AB 1024) was amended to include a new subdivision that would provide the exception noted in the federal code 1621 (d) and allow an undocumented immigrant to be granted a law license. The bill was passed by a majority vote in both the California State Senate and State Assembly. Governor Jerry Brown signed it in the following month, and the new addition became subdivision (b) of the California Business and Professions Code 6064, effective January 1, 2014.<sup>11</sup>

Attorney General Kamala Harris' supplemental brief to the Garcia matter pointed to the new law:

*"Through AB 1024, the Legislature has expressly enlarged the power of this court to admit attorney applicants to the State Bar of California despite the applicant's lack of full immigration status. The passage of the new statute fully resolves the concerns raised by the federal government in opposition to admitting Mr. Garcia to the State Bar."*<sup>12</sup>

A footnote to her supplemental brief indicated that the federal government (in its own amicus brief) indicates that "employment authorization" is separate and distinct from the granting of a law license and that the issue of employment was not then before the court.<sup>13</sup>

### **Good Moral Character**

As noted earlier, part of the application process for admission to the California State Bar is a determination by the Bar of "good moral character," which was considered by the Court. The main opinion stated that Garcia, after an "extensive employment history, and past activities" supported by numerous letters concerning Garcia's "outstanding moral character" and "contributions to the community" was found to have the "requisite good moral character to qualify for admission to the State Bar." The Court also recognized that Garcia was a "hard-working, tax-paying, individual who has assisted many others and whose applications is supported by many members of the community, by past teachers, and by those whom he has worked." But it also noted that his conduct was not "entirely flawless."

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<sup>11</sup>Procedural note: Because of the new addition to 6064, the matter submitted to the Court was vacated and then resubmitted on the day following its effective date – January 2, 2014 – the day of Court's ruling. Following the enactment of the revised code, the Court had instructed the various amici curiae to file supplemental briefs.

<sup>12</sup>Kamala Harris' 2013 supplemental brief may be read at: <http://www.courts.ca.gov/documents/33-s202512-amicus-curiae-kamala-harris-supp-brief-111513.pdf>

<sup>13</sup> The amicus 2012 brief of the United States may be read at: <http://www.courts.ca.gov/documents/20-s202512-amicus-united-states-america-080312.pdf>

The flaw to which the Court referred involved a job Garcia had obtained at age 17, wherein he was obligated to provide an alien registration number, which he did not have, as well as attesting to lawful permanent residence, which was not then the case. This fact was eventually made available to the Committee of Bar Examiners. The Committee, after examining the entire record, determined that the “it believed that Garcia was sincerely remorseful for his past misconduct and (that) his delay in disclosing the document was a product of his reliance upon the erroneous advice of his counsel, and concluded that under the circumstances the conduct did not reflect moral turpitude.”<sup>14</sup>

The Court also considered whether an undocumented immigrant could take the oath of office, which is required for attorneys, as well as the contention that by “simply being in this country without authorization,” is itself a violation of federal immigration law. Citing California cases, the Court wrote:

*We conclude the fact that an undocumented immigrant is present in the United States without lawful authorization does not itself involve moral turpitude or demonstrate moral unfitness so as to justify exclusion from the State Bar, or prevent the individual from taking an oath promising faithfully to discharge the duty to support the Constitution and laws of the United States and California.*

As a result, Sergio C. Garcia was admitted by the California Supreme Court to the practice of law in the State of California on January 2, 2014. But that admission is not the complete story.

### **A License and the Ability to Work**

In June 2015 Garcia, was finally granted his “green card” by federal authorities – more than 20 years after his initial application -- which allows him to work and live legally in the United States.<sup>15</sup> However, in the Garcia, the issue of his ability to work in California was considered by

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<sup>14</sup>This discussion is found in footnote 5 in the main case. As a comparison, in the same year Garcia’s case was considered, another intriguing case of that came before the California Supreme Court that considered the issue of “good moral character,” and is well worth the read. In that case, the application of Stephen Randall Glass, who came to popular notoriety in the 1990s for “fabricating material for more than 40 articles for The New Republic,” and which later became the subject of the 2003 movie “Shattered Glass,” was considered. In that case, the applicant at that time was denied a license as “His evidence did not establish that he engaged in truly exemplary conduct over an extended period,” and thus, the court determined that Glass had not demonstrated “rehabilitation and fitness for the practice of law.” The citation is 58 Cal.4th 500 58 Cal.4th 500; 316 P.3d 1199; 167 Cal. Rptr. 3d 87 and may be read via: <http://www.lexisnexis.com/clients/CACourts/> (public access to older cases in the California courts are available via this site).

<sup>15</sup> Associated Press, June 4, 2015, “Immigrant California lawyer finally gets green card” (accessed via Yahoo at: <https://www.yahoo.com/news/apnewsbreak-california-lawyer-gets-green-card-battle-190027589.html?ref=gs>

the Court. The Court at the time was considering the fact that Garcia did not yet have a green card.<sup>16</sup>

In response to one *amicus curiae* brief in the Garcia case, the court addressed whether, because of an undocumented immigrant's inability to be lawfully employed in the United States, that it would be improper to grant a law license in the first place. The Court noted that the many *amici curiae* all agreed that if an undocumented immigrant were allowed a law license, employment with a "law firm, corporation, or governmental entity" would be precluded.<sup>17</sup> And they agreed that work on a "pro bono" basis, i.e., free volunteer work would not violate federal law. However there was disagreement as to whether an undocumented immigrant with a license could work as an "independent contractor" or as a sole practitioner.

The Court – while recognizing the limitations of federal law – stated that "...the inability to represent California residents in some legal matters (did) not necessarily preclude all possible uses of a law license." It argued instead that under the California Rules of Professional Conduct, such attorneys would be obligated not to act as attorneys for clients where restricted on ethical or legal grounds. Therefore, the court dispensed with the issue whether it would be improper to deny a California law license on the basis of legal employability. However, it was not exactly clear about what granting a license to an undocumented person would mean for subsequent employment. Justice Cantil-Sakauye wrote:

*As this bill analysis accurately recognizes, this court's granting of a law license to undocumented immigrants would not override or otherwise affect the federal limitations upon the employment of undocumented immigrants. Nonetheless, for a number of reasons we conclude that existing federal limitations on the employment of undocumented immigrants do not justify excluding undocumented immigrants from admission to the State Bar.*

However, the federal government in its *amicus brief* – the Court noted – commented that "federal provisions governing employment by aliens is the responsibility of the federal government," - not the province of a state court. Thus, the state court should not "attempt to resolve any question about the types of legal services that Mr. Garcia may provide if granted a license." The situation for Garcia, therefore, is different for those individuals who qualified under DACA (Deferred Action for Childhood Arrivals), at least in California, as described in the next section of this chapter.<sup>18</sup>

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<sup>16</sup>Jennifer Medina, "Allowed to Join the Bar, but Not to Take a Job," *New York Times*, January 2, 2014, Available at <http://www.nytimes.com/2014/01/03/us/immigrant-in-us-illegally-may-practice-law-california-court-rules.html>

<sup>17</sup>The Court referenced 8 U.S.C. section 1324(a)(1)(A).

<sup>18</sup>DACA was established by President Obama to deal with individuals brought illegally into the U.S. as children. At this writing, the fate of the DACA program under incoming President Donald Trump is unknown.

## DACA Cases in California and Elsewhere

In January 2015, another individual with the status of an undocumented immigrant was admitted to California's Bar. Vanessa Pumar, whose own long struggle to achieve her dream was realized as she was sworn in as an attorney in the court of U.S. District Judge Jesus G. Bernal, in Riverside, California. Vanessa Pumar was born in Venezuela and came to the U.S. with her parents at the age of 12. Her situation was different from Garcia's in that she was the first to be admitted to the Bar under the provisions of DACA.<sup>19</sup> Under a list of DACA guidelines, a recipient must have been under age 16 at the time of arrival in the United States, which Pumar was, and, which Garcia before her, was not.<sup>20</sup>

Each state that considers the issue will first encounter federal statute 1621, and, as the Garcia and Pumar cases illustrate, it remains to be seen how each state will approach the issue and what the result will be. In New York, for example, in 2016, Cesar Vargas - who was born in Mexico – did receive admission to that state's bar.<sup>21</sup> Vargas, like Pumar in California, benefitted under the auspices of the DACA guidelines established by the U.S. Department of Homeland Security. But unlike California, legislation to create a state law in New York to circumvent federal rule 1621 via the 1621(d) provision, had failed to pass in the previous year. However, the New York Court of Appeals, that state's highest court, found a constitutional flaw in 1621.<sup>22</sup>

*We hold that the narrow reading of 8 USC section 1621(d), so as to require a state legislative enactment to be the sole mechanism by which the State of New York exercises its authority granted in 8 USC section 1621(d) to opt out of the restrictions on the issuance of licenses imposed by 8 USC section 1621(a), unconstitutionally infringes on the sovereign authority of the State to divide power among its three coequal branches of government.*<sup>23</sup>

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<sup>19</sup>Roxana Kopetman, "Former Irvine resident becomes lawyer, despite her legal status," *Orange County Register*, January 28, 2015. Available at <http://www.ocregister.com/articles/pumar-649559-law-immigration.html>. John Cádiz Klemack, "Undocumented Immigrant Becomes Licensed Attorney" (includes news video), *NBCLA.com*, January 29, 2015. Available at: <http://www.nbclosangeles.com/news/local/Undocumented-Immigrant-Becomes-Licensed-Attorney-290291471.html>.

<sup>20</sup>DACA guidelines may be reviewed on the U.S. Citizen and Immigration Services site at: <https://www.uscis.gov/humanitarian/consideration-deferred-action-childhood-arrivals-daca#guidelines>

<sup>21</sup>Liz Robbins, "New York Court Rules for Immigrant in Fight to Become Lawyer" *New York Times*, June 4, 2015. Available at: <http://www.nytimes.com/2015/06/05/nyregion/undocumented-immigrant-may-work-as-a-lawyer-new-york-court-rules.html>. Liz Robbins, "An Immigrant's Four-Year Fight to Become a Lawyer Ends in Celebrations," *New York Times*, February 3, 2016. Available at: <http://www.nytimes.com/2016/02/04/nyregion/immigrants-4-year-legal-fight-to-become-a-lawyer-ends-in-celebration.html>.

<sup>22</sup>Unlike most states, New York's highest court is the Court of Appeals, whereas its lower courts are referred to as the New York Supreme Court.

<sup>23</sup>In the Matter of Cesar Adrian Vargas:  
<http://www.courts.state.ny.us/courts/ad2/calendar/webcal/decisions/2015/D45607.pdf>

So, not only did the New York Court assert the final state authority, like California, to issue law licenses, it furthermore asserted its “sovereignty” to “opt out of the federal restrictions imposed by 1621(a) to the limited extent that those restrictions apply to the admission of attorneys to the practice of law in the State of New York.”<sup>24</sup>

In Florida, however, applicant Jose Godinez-Samperio was *denied* admission to that state’s bar because of the federal law. In fact, in 2014, Florida’s Supreme Court held “that unauthorized immigrants are ineligible for admission to the Florida Bar. Applicants are required to demonstrate that they are legally present in the United States.”<sup>25</sup> At that time in Florida state legislators had not passed the requisite law as provided in 1621(d).<sup>26</sup> But, the state finally did pass the required law, and Godinez-Samperio was granted a license in September 2014.<sup>27</sup>

### **Back to the Future: Posthumous Admission to the Bar**

On Monday, March 16, 2015, a man named Hong Yen Chang was admitted to the California State Bar – more than a century after the California Supreme Court denied him his license to practice law in the state.<sup>28</sup> Despite this setback, Chang went on to become a successful banker and diplomat, retiring in Berkeley, California. Hong Yen Chang came to the United States in 1872. He earned his undergraduate degree from Yale and went on to earn a law degree from Columbia University in 1886.

Upon his first application to the New York Bar, he was denied due to lack of citizenship. But later in the same year he was granted certificate of naturalization by a New York judge, despite the federal Chinese Exclusion Act of 1882 which barred naturalization of Chinese. With his certificate, Chang was then admitted, following legislation in New York that would allow Chang to reapply to the New York State Bar. As a result, Hong Yen Chang became the first Chinese lawyer in the United States. Chang then moved to California, with the intention of working as a

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<sup>24</sup>Cristian Farias, “César Vargas Just Became New York’s First Undocumented Lawyer,” *New York Magazine*, June 5, 2015. Available at: <http://nymag.com/daily/intelligencer/2015/06/new-york-just-got-its-first-undocumented-lawyer.html>.

<sup>25</sup><http://www.floridasupremecourt.org/decisions/2014/sc11-2568.pdf>.

<sup>26</sup>Roque Planas, “First Undocumented Immigrant ‘F\*\*king Finally’ Allowed to Practice Law in New York,” *Huffington Post*, June. 4, 2015. Available at: [http://www.huffingtonpost.com/2015/06/04/undocumented-law-new-york\\_n\\_7510172.html](http://www.huffingtonpost.com/2015/06/04/undocumented-law-new-york_n_7510172.html).

<sup>27</sup>*Florida Bar News*, December 15, 2014 “Godines-Samperio Finally Becomes a Florida Lawyer.” Available at: [https://www.floridabar.org/\\_85256AA9005B9F25.nsf/0/3A670C910F44826185257DA8004EBAF0?OpenDocument](https://www.floridabar.org/_85256AA9005B9F25.nsf/0/3A670C910F44826185257DA8004EBAF0?OpenDocument).

<sup>28</sup>The story of Hong Yen Chang is recounted in Maura Dolan, “Ruling gives posthumous law license to victim of anti-Chinese 1890s,” *Los Angeles Times*, March 17, 2015. Available at: <http://www.latimes.com/local/california/la-me-chinese-lawyer-20150317-story.html>.



lawyer in San Francisco, but his application to the California State Bar was denied. The Court's justification for denying membership was the federal Chinese Exclusion Act.<sup>29</sup>

More than a century later, in 2011, under the guidance of UC-Davis law professor Gabriel Chin, students from Davis' Asian Pacific American Law Association began work on reversing the 1890 California ruling. The Association eventually filed the posthumous motion to have Chang's case considered. In response, the California Supreme Court, under its Chief Justice Cantil-Sakauye, ruled in favor of Chang in a decision that cited the Garcia case:

*Even if we cannot undo history, we can acknowledge it and, in so doing, accord a full measure of recognition to Chang's path-breaking efforts to become the first lawyer of Chinese descent in the United States. The people and the courts of California were denied Chang's services as a lawyer. But we need not be denied his example as a pioneer from a more inclusive legal profession. In granting Hong Yen Chang posthumous admission to the California Bar, we affirm his rightful place among the ranks of persons deemed qualified to serve as an attorney and counselor at law in the courts of California.*<sup>30</sup>

While Chang has no direct descendants alive today, he does have relatives living in California. Chang's great-grandniece – herself a prominent California attorney – said, "The family was troubled that it happened, but we didn't ever imagine there was anything we could do about it... We are so excited, you have no idea."<sup>31</sup>

### **"Alien": A Word on Terminology**

Interestingly, the very first note of the Garcia Opinion takes up the matter – at length – of terminology, specifically what to call a person in Garcia's situation. The opinion notes that the words "unlawful," "unauthorized," "Illegal aliens" or "immigrants" have been generally used. But both the U.S. Supreme Court and the California Legislature have used "undocumented immigrant," thus avoiding "problematical connotations of alternative terms."

However, in his concurring opinion, California Supreme Court Justice Ming W. Chin reminded the court of a 2010 California Supreme Court opinion in which the court "unanimously rejected" the term "undocumented immigrant," for the term "unlawful alien."<sup>32</sup> Justice Chin also points out that both the word "alien" and phrase "not lawfully present" are used in the federal and state statutes at issue in this case (8 U.S.C. section 1621(d) and California Business and Professions Code, section 6064, sub-div. (b)). While commenting that "undocumented

<sup>29</sup>The Act was repealed in 1943 when China was an ally of the United States during World War II.

<sup>30</sup>The Court's opinion may be read online at: <http://www.courts.ca.gov/opinions/archive/S223736.PDF>.

<sup>31</sup>Maura Dolan, "Ruling gives posthumous law license to victim of anti-Chinese 1890s," *Los Angeles Times*, March 17, 2015. Available at: <http://www.latimes.com/local/california/la-me-chinese-lawyer-20150317-story.html>.

<sup>32</sup> *Martinez v. Regents of the University of California*, 50 Cal. 4<sup>th</sup>.



immigrant” in his opinion may be “vague” and “not used in the relevant statutes,” he did recognize that terms such as “illegal alien,” may be seen as “pejorative” – although “unlawful alien” may not sound any less so. Ultimately, Chin defers to the discretion of the opinion’s author, Chief Justice Tani Cantil-Sakauye, on terminology in this specific case.

And, interest in the terminology was not limited to the courts. It was also appearing on the legislative front. Early in 2015, California Senate Bill (SB 432) was introduced by state senator Tony Mendoza (D-Artesia) that would remove the term “alien” from the state’s labor code. The proposed bill would accomplish this by repealing sections 1725 and 2015 of the California Labor Code related to public works employment.<sup>33</sup>

“Alien is now commonly considered a derogatory term for a foreign-born person and has very negative connotations,” said Mendoza prior to approval of the bill by Governor Brown in August 2015.<sup>34</sup> In the background history provided in the commentary to the bill, it is recalled that the state Legislature had, in 1937, enacted a number of provisions “regarding the employment of ‘aliens,’” most of which were repealed in 1970. But, the term “alien” still existed within the Labor Code.

In a *Los Angeles Times* story reporting on the passage of the bill, Kevin R. Johnson, dean of the UC Davis School of Law, commented on “growing national sentiment” that the use of the word is inappropriate although it still exists in federal immigration law.<sup>35</sup> Johnson noted that “the concern is that the use of the word ‘alien’ would dehumanize the people affected” and lead to “lack of protections under the law.” His point was that words can, and do, matter – in the law, legislation and individual lives. With the uncertainty over immigration matters generated by the 2016 presidential election, the words of officials – not just of the law – may also matter to individuals such as Sergio C. Garcia when it comes to practicing law or working in any occupation.

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<sup>33</sup> The text, legislative history and analysis of SB-432 Public works: aliens (2015-2016) may be found at: [https://leginfo.legislature.ca.gov/faces/billTextClient.xhtml?bill\\_id=201520160SB432](https://leginfo.legislature.ca.gov/faces/billTextClient.xhtml?bill_id=201520160SB432)

<sup>34</sup> California Senator Tony Mendoza website press release, May 1, 2015: <http://sd32.senate.ca.gov/news/512015-bill-remove-term-%E2%80%9Calien%E2%80%9D-california-labor-code-approved-state-senate>

<sup>35</sup> Patrick McGreevy, “Gov. Brown doesn’t want California to use this word for immigrants,” *Los Angeles Times*, August 10, 2015. Available at: <http://www.latimes.com/local/political/la-me-pc-gov-jerry-brown-signs-bills-to-help-immigrants-20150810-story.html>